

**H.R. _____, A BILL TO ENHANCE FEDERAL
AND STATE ENFORCEMENT OF FRAUDULENT
PATENT DEMAND LETTERS**

HEARING
BEFORE THE
SUBCOMMITTEE ON COMMERCE, MANUFACTURING,
AND TRADE
OF THE
COMMITTEE ON ENERGY AND
COMMERCE
HOUSE OF REPRESENTATIVES
ONE HUNDRED THIRTEENTH CONGRESS
SECOND SESSION

MAY 22, 2014

Serial No. 113-149



Printed for the use of the Committee on Energy and Commerce
energycommerce.house.gov

U.S. GOVERNMENT PUBLISHING OFFICE

95-698

WASHINGTON : 2015

For sale by the Superintendent of Documents, U.S. Government Publishing Office
Internet: bookstore.gpo.gov Phone: toll free (866) 512-1800; DC area (202) 512-1800
Fax: (202) 512-2104 Mail: Stop IDCC, Washington, DC 20402-0001

COMMITTEE ON ENERGY AND COMMERCE

FRED UPTON, Michigan
Chairman

RALPH M. HALL, Texas
JOE BARTON, Texas
Chairman Emeritus
ED WHITFIELD, Kentucky
JOHN SHIMKUS, Illinois
JOSEPH R. PITTS, Pennsylvania
GREG WALDEN, Oregon
LEE TERRY, Nebraska
MIKE ROGERS, Michigan
TIM MURPHY, Pennsylvania
MICHAEL C. BURGESS, Texas
MARSHA BLACKBURN, Tennessee
Vice Chairman
PHIL GINGREY, Georgia
STEVE SCALISE, Louisiana
ROBERT E. LATTA, Ohio
CATHY McMORRIS RODGERS, Washington
GREGG HARPER, Mississippi
LEONARD LANCE, New Jersey
BILL CASSIDY, Louisiana
BRETT GUTHRIE, Kentucky
PETE OLSON, Texas
DAVID B. MCKINLEY, West Virginia
CORY GARDNER, Colorado
MIKE POMPEO, Kansas
ADAM KINZINGER, Illinois
H. MORGAN GRIFFITH, Virginia
GUS M. BILIRAKIS, Florida
BILL JOHNSON, Missouri
BILLY LONG, Missouri
RENEE L. ELLMERS, North Carolina

HENRY A. WAXMAN, California
Ranking Member
JOHN D. DINGELL, Michigan
Chairman Emeritus
FRANK PALLONE, JR., New Jersey
BOBBY L. RUSH, Illinois
ANNA G. ESHOO, California
ELIOT L. ENGEL, New York
GENE GREEN, Texas
DIANA DEGETTE, Colorado
LOIS CAPPS, California
MICHAEL F. DOYLE, Pennsylvania
JANICE D. SCHAKOWSKY, Illinois
JIM MATHESON, Utah
G.K. BUTTERFIELD, North Carolina
JOHN BARROW, Georgia
DORIS O. MATSUI, California
DONNA M. CHRISTENSEN, Virgin Islands
KATHY CASTOR, Florida
JOHN P. SARBANES, Maryland
JERRY MCNERNEY, California
BRUCE L. BRALEY, Iowa
PETER WELCH, Vermont
BEN RAY LUJAN, New Mexico
PAUL TONKO, New York
JOHN A. YARMUTH, Kentucky

SUBCOMMITTEE ON COMMERCE, MANUFACTURING, AND TRADE

LEE TERRY, Nebraska
Chairman

LEONARD LANCE, New Jersey
Vice Chairman
MARSHA BLACKBURN, Tennessee
GREGG HARPER, Mississippi
BRETT GUTHRIE, Kentucky
PETE OLSON, Texas
DAVE B. MCKINLEY, West Virginia
MIKE POMPEO, Kansas
ADAM KINZINGER, Illinois
GUS M. BILIRAKIS, Florida
BILL JOHNSON, Missouri
BILLY LONG, Missouri
JOE BARTON, Texas
FRED UPTON, Michigan, *ex officio*

JANICE D. SCHAKOWSKY, Illinois
Ranking Member
JOHN P. SARBANES, Maryland
JERRY MCNERNEY, California
PETER WELCH, Vermont
JOHN A. YARMUTH, Kentucky
JOHN D. DINGELL, Michigan
BOBBY L. RUSH, Illinois
JIM MATHESON, Utah
JOHN BARROW, Georgia
DONNA M. CHRISTENSEN, Virgin Islands
HENRY A. WAXMAN, California, *ex officio*

CONTENTS

	Page
Hon. Lee Terry, a Representative in Congress from the State of Nebraska, opening statement	1
Prepared statement	2
Hon. Fred Upton, a Representative in Congress from the State of Michigan, prepared statement	87

WITNESSES

Hon. Jared Polis, a Representative in Congress from the State of Colorado	3
Prepared statement	6
Tom Marino, a Representative in Congress from the State of Pennsylvania	9
Prepared statement	11
Lois Greisman, Associate Director, Bureau of Consumer Protection, on Behalf of Federal Trade Commission	14
Prepared statement	17
Answers to submitted questions	95
Wendy Morgan, Chief of the Public Protection Division, Office of the Attorney General of Vermont	25
Prepared statement	27
Answers to submitted questions	100
Adam Mossoff, Professor of Law, George Mason University	39
Prepared statement	41
Robert Davis, Counsel, Venable LLP, on Behalf of Stop Patent Abuse Now Coalition	48
Prepared statement	50
Jon Potter, President and Co-Founder, Application Developers Alliance	53
Prepared statement	55
Answers to submitted questions	104
Alex Rogers, Senior Vice President and Legal Counsel, Qualcomm	62
Prepared statement	64
Answers to submitted questions	107

SUBMITTED MATERIAL

Statement of the National Association of Federal Credit Unions, submitted by Mr. Terry	88
Statement of the National Association of Realtors, submitted by Mr. Terry	89
Statement of the State of Nebraska Attorney General, submitted by Mr. Terry	90
Statement of Main Street Patent Coalition, submitted by Mr. Terry	93

**H.R. ———, A BILL TO ENHANCE FEDERAL
AND STATE ENFORCEMENT OF FRAUDU-
LENT PATENT DEMAND LETTERS**

THURSDAY, MAY 22, 2014

HOUSE OF REPRESENTATIVES,
SUBCOMMITTEE ON COMMERCE, MANUFACTURING, AND
TRADE,
COMMITTEE ON ENERGY AND COMMERCE,
Washington, DC.

The subcommittee met, pursuant to call, at 9:15 a.m., in room 2123, Rayburn House Office Building, Hon. Lee Terry (chairman of the subcommittee) presiding.

Present: Representatives Terry, Lance, Blackburn, Harper, Olson, McKinley, Kinzinger, Bilirakis, Johnson, Long, Sarbanes, McNeerney, Welch, and Barrow.

Staff Present: Charlotte Baker, Deputy Communications Director; Kirby Howard, Legislative Clerk; Brian McCullough, Senior Professional Staff Member, Subcommittee on Commerce, Manufacturing and Trade; Paul Nagle, Chief Counsel, Subcommittee on Commerce, Manufacturing and Trade; Shannon Weinberg Taylor, Counsel, Subcommittee on Commerce, Manufacturing and Trade; Graham Dufault, Subcommittee on Commerce, Manufacturing and Trade Policy Coordinator; Michelle Ash, Minority Chief Counsel; and Will Wallace, Minority Professional Staff Member.

**OPENING STATEMENT OF HON. LEE TERRY, A REPRESENTA-
TIVE IN CONGRESS FROM THE STATE OF NEBRASKA**

Mr. TERRY. For our panel and for our witnesses, we do expect to vote somewhere between 10:00 and 10:15. So I am just going to say good morning to everyone, and this is a really important hearing because of the numerous complaints that we have received, particularly from end users regarding the perceived fraudulent demands on patent infringements.

The committee has taken an approach to be—what would be the right term—intellectual about this, realizing that there are First Amendment implications, as well as we do not want to make it more difficult for valid patent holders to pursue their remedies when there is a violation, and so therefore, this is really the art and science of wording.

And that is why we have this hearing today is to get the experts to help us make sure that we have the needle thread appropriately so that we don't injure or make it more difficult for valid patent

holders of any size, but that we are able to curtail the abuses that we see occurring.

[The prepared statement of Mr. Terry follows:]

PREPARED STATEMENT OF HON. LEE TERRY

Good morning and welcome to this morning's legislative hearing. Today, we examine a discussion draft of legislation to address the growing problem of unfair and deceptive patent demand letters.

The policy goals we consider here today are not a matter of partisan politics. We can all agree that certain actors are operating a successful business model of defrauding others under the guise of seeking compensation for alleged patent infringement—and that this practice should be addressed.

Thanks to these fraudsters, small businesses all over the United States are learning quickly that their everyday activities may or may not be infringing a patent that a mysterious company may or may not own. These small businesses are also learning not very much about how they might be infringing, but that they can escape a lawsuit if a license fee is paid.

In one example, home builders recently became the favored victim of a patent assertion entity with the rights to a wood de-humidifying process. According to this assertion entity's letters, several home builders in the Pacific Northwest likely infringed on its patent because . . . well, because the recipients of the letters build homes.

The patent at issue consists of a process of controlling moisture inside a building as it is being built. You would have no idea what exactly that process is from reading the letter. You would also have no idea what the recipient of the letter was doing that might implicate the patent. The letter is clear, however, that there is an option to pay the license fee, or—somewhat ominously—be deemed to “refuse to enter into a license for the patented moisture removal process.”

As an initial matter, I note that some believe the problem is not systemic, and therefore federal legislation is not sufficiently justified. I happen to disagree; we have heard from too many businesses that are desperate for relief, and I believe there is a narrow path forward. It's time we discussed the nuts and bolts of how we accomplish the task before us, and I thank the witnesses for being here today to do just that.

There is no doubt—given the competing considerations outlined by stakeholders thus far—that we will have to thread the proverbial needle with this legislation.

For example, some argue that the Federal Trade Commission should have to prove that false statements are made with some level of knowledge that they are false in order to bring an enforcement action.

Moreover, prohibiting speech that isn't false and compelling certain disclosures may implicate the First Amendment, and I intend for this legislation to withstand a constitutional challenge.

The scope of the legislation is also a point of contention. Our purpose on this issue should be to protect those who are unable to defend themselves and who would benefit most from truthful statements and more detail.

On the other hand, we must be careful not to implicate letters sent between two sophisticated patent owners, especially those with prior business relationships and accustomed to dealing with these issues. If these letters are part of our legislation, we invite gamesmanship on the part of the would-be licensee and risk devaluing patents generally.

Lastly, our draft legislation includes a rebuttable presumption that protects those who send demand letters from enforcement actions for technical violations of the disclosure requirements.

This falls short of a safe harbor as to all aspects of the bill, but provides limited shelter for letters that attempt to make the right disclosures, where an enforcer may believe those disclosures are inadequate. I expect that there will be diverse opinions disagreement on this provision as well.

Once again, I thank the witnesses for their participation and I look forward to lively debate on these and other issues surrounding the bill.

Mr. TERRY. At this point, I will yield back my time and recognize Jerry for an opening statement, unless you waive.

Mr. MCNERNEY. No, I will just say a few words. Thank you, Mr. Chairman.

Mr. TERRY. OK. So you are recognized for your 5 minutes.

Mr. MCNERNEY. Thank you, witnesses, for coming this morning. I am a patent holder. I have a couple patents. I do have concerns of patent violations, but I also understand the challenge of making sure that we don't have a patent system where companies, entities are able to gain the system because that hurts everyone except the gamers. And threading that needle is going to be a challenge. I appreciate the chairman's viewpoint on this to protect the patent holders as well as providing the right words in the law that make this a viable law.

So I am going to be brief and yield back, Mr. Chairman, and I thank you for holding this hearing.

Mr. TERRY. I appreciate that. And now I will recognize, we have the esteemed first panel, who are Members of Congress that are also active on patent and patent abuse issues. Mr. Polis from Colorado, and Mr. Marino.

And Mr. Polis, you will be first. You are recognized for your 5 minutes, although you said you needed 40. If we can compromise at 5. You are recognized.

**STATEMENT OF THE HON. JARED POLIS, A REPRESENTATIVE
IN CONGRESS FROM THE STATE OF COLORADO**

Mr. POLIS. Thank you, Mr. Chairman, in the proud tradition of compromise. Thank you, Chairman Terry, Acting Ranking Member McNerney for allowing me the opportunity to testify on this important topic of patent demand letter reform. I deeply appreciate, on behalf of my constituents, the attention your committee is devoting to the issue of abuse of demand letters.

As an entrepreneur and former venture capital investor, like my colleague, Mr. McNerney, an inventor of several patented inventions, I got to experience from several perspectives the challenges of starting and running a small business. Today these challenges are exacerbated by patent trolls who prey on our core job creators including many startups in my home district in Colorado by sending misleading and scary demand letters without basis.

Patent trolls increase the cost of doing business and cause small businesses to shell out millions in legal fees or settlement fees to address illegitimate and unfounded claims. While many of these patents should never have been granted in the first place, but since they have, one of the ways to crack down on patent trolls is by requiring demand letter transparency and allowing enforcement against bad actors.

Last November, I was pleased to introduce, along with my colleague, Representative Marino, as well as Representative Deutch, a bipartisan comprehensive bill that accomplished these goals, the Demand Letter Transparency Act. Our bill would require certain patent holders to disclose information relating to the patent in their demand letters and file their letters in a searchable and accessible public registry maintained by the PTO. Our bill truly would help prevent trolls from hiding behind anonymity, empower defendants to take action together and share information as well as alert regulatory authorities and the PTO about frivolous enforcement of patents.

Let me be clear, addressing abuse of patent demand letters is only a part of a much larger issue. Our patent system, in many

ways, was designed to protect physical innovation, machines and contraptions and now attempts are being made to apply it to apps and the Cloud and digital innovation.

Much more needs to be done to ensure that the innovations of tomorrow have the same protections as the innovations as yesterday without casting a power on the ongoing innovations of our economy. I was sad to hear Senator Leahy's recent announcement with regard to the patent bill in the Senate, but I want to remind this committee of the urgency that we have to find common ground and bring our patent system into the 21st century.

While I wish the discussion draft took a more comprehensive approach to combating abusive demand letters, I certainly understand the limited jurisdiction of this committee, and I am encouraged that this committee is moving forward on the issues under its jurisdiction. However, I also want to point out, with regard to the committee's proposal, some language that may inadvertently actually take us backwards in addressing the troll problem at the pre-litigation stage.

First, I am concerned that the bill may inadvertently limit the FTC's Section 5 authority to target harmful behaviors. The FTC already has enforcement authority to go after certain entities who are engaging in unfair and deceptive practices by sending abusive demand letters. I commend the committee for its inclusion of a savings clause in its discussion draft, which is a great improvement over the original draft, but I believe that the language may not be sufficient to preserve the FTC's existing Section 5 authority.

By delineating a list of unfair and deceptive acts or practices in the bill, the legislation may actually limit the ability of the FTC to target other unnamed harmful behaviors and unforeseen abusive behaviors. So to ensure this legislation does not foreclose the FTC's existing enforcement authority, I urge the committee to include a catch-all provision that would allow the FTC to bring actions to address other harmful behaviors than aren't expressly listed in the legislation.

Second, I am concerned with the draft's broad preemption clause, which may inhibit state attorney generals from seeking civil penalties against bad actors. The United States have passed strong laws that are pro-innovation, prohibiting abusive demand letters. 42 State AGs have explicitly stated their desire for Federal demand letter reform along with concurrent State authority.

Until we can act decisively at the Federal level, I hope that this body can support the actions that States are taking to protect their small businesses and entrepreneurs. I am thus concerned that this discussion draft may strip State AGs of an important tool that we need to combat bad actors.

Third, I have concerns that the rebuttable presumption language may create a loophole. The inclusion of this language may place a large burden on demand letter recipients and the FTC to prove their case.

Finally, I am concerned that the bill's scope is only limited to systems integrators, consumers and end users. I am hopeful we can expand the bill's definition to protect all recipients of demands by bad actors. In the real world, these examples include restaurants, app developers, retail software or services.

Thank you, again, for allowing me to testify today. I truly believe that the FTC, under the jurisdiction of this committee, does have a critical role to play with regard to improving the climate for entrepreneurship across our country. I greatly appreciate your attention to patent demand letter reform, and I look forward to working with you on this legislation.

Mr. TERRY. Thank you.

[The prepared statement of Mr. Polis follows:]

Congressman Jared Polis: Testimony Before the House Energy and Commerce Subcommittee on Commerce, Manufacturing, and Trade

Hearing on H.R. _____, a bill to enhance federal and state enforcement of fraudulent patent demand letters

Thank you Chairman Terry, Ranking Member Schakowsky and Members of the Subcommittee for allowing me the opportunity to testify on the important topic of patent demand letter reform. I greatly appreciate the attention the Committee has devoted to the issue of abusive patent demand letters.

As an entrepreneur and former venture capital investor, I experienced first-hand the challenges of starting and running small businesses. These challenges are exacerbated by the patent trolls who prey on our core job creators – including many startups in my District- by sending fraudulent patent demand letters. Patent trolls increase the cost of doing business and cause small businesses to shell out millions in legal or settlement fees to address illegitimate claims.

One of the ways to crack down on patent trolls is by requiring demand letter transparency and allowing enforcement against bad actors. Last November, I was pleased to introduce, along with Representatives Tom Marino and Ted Deutch, a bipartisan comprehensive bill that accomplished both of these goals, *The Demand Letter Transparency Act*.

Our bill would require certain patent holders to disclose information relating to the patent in their demand letters and file their letters in a public registry maintained by the PTO that is searchable and accessible. Our bill would prevent trolls from hiding behind anonymous shell companies; empower defendants to take collective action and share information; and alert regulatory authorities and the Patent and Trademark Office about patents that are being frivolously asserted.

But let me be clear: addressing abusive patent demand letters is only part of a much larger issue. Our antiquated patent system was designed to protect machines and contraptions; not apps and clouds. There is much that needs to be done to ensure that the innovations of tomorrow have the same protections as the inventions of yesterday. With Senator Leahy's recent announcement that he is taking the patent bill off the Committee's agenda - I

want to remind the Committee that we can still find common ground to bring our patent system into the 21st century. Further, if the House recognizes the dangers of the patent troll business model and fixes our patent system in a strong, bipartisan manner, it just may send a message to the Senate that the time to act and protect our nation's small business is now.

While I wish the Discussion Draft, took a more comprehensive approach to combating abusive demand letters as *The Demand Letter Transparency Act* does, I certainly understand the limited jurisdiction of this Committee and am encouraged that the Committee is moving forward on this issue. However, I am concerned that in an attempt to address the issue of abusive demand letters, the Committee's proposal may have inadvertently taken us backwards on addressing the troll problem at the pre-litigation stage.

First, I am concerned that the bill may inadvertently limit the FTC's Section 5 authority to target harmful behaviors. The FTC already has enforcement authority to go after certain entities who are engaging in unfair and deceptive practices by sending abusive demand letters – most recently evidenced by their investigation of *MPHJ*.

I commend the Committee for its inclusion of a savings clause in its Discussion Draft - a great improvement over the original draft language. However, I believe that the language may not be sufficient to preserve the FTC's Section 5 authority. I am troubled that by delineating an exhaustive list of unfair or deceptive acts or practices in the bill, the underlying legislation may limit the ability of the FTC to target other harmful behaviors and unforeseen abusive behaviors. To ensure that this legislation does not foreclose the FTC's enforcement authority, I urge the Committee to include a catch-all provision that would allow the FTC to bring actions to address other harmful behaviors that are not expressly listed in the legislation.

Second, I am concerned with the Draft's broad preemption clause – which may inhibit State Attorney Generals from seeking civil penalties against bad actors. Nine states have passed strong laws prohibiting abusive demand letters; many more are in the process of doing so. And forty-two State Attorneys General have expressly stated their desire for federal demand-letter reform and they wanted that with concurrent state authority. Until we can act at the federal level, we must support the action that the states are taking to protect their small businesses. I am thus concerned that this

Discussion Draft may strip state AGs of this important tool to combat bad actors.

Third, I have concerns that the rebuttable presumption language may create a large loophole trolls can climb through. The inclusion of this language may place a large burden on demand letter recipients and the FTC to prove their case.

Finally, I am troubled that the bill's scope is only limited to "systems integrator" "consumers" and "end users." I am hopeful that we can expand the bill's definition to protect all recipients of demands by bad actors.

Thank you again for allowing me to testify today. I greatly appreciate your attention to the issue of addressing patent troll demand letter and look forward to working with you on this legislation.

Mr. TERRY. Gentleman from Pennsylvania is now recognized for 5 minutes.

**STATEMENT OF THE HON. TOM MARINO, A REPRESENTATIVE
IN CONGRESS FROM THE STATE OF PENNSYLVANIA**

Mr. MARINO. Thank you, chairman, and thank you acting ranking member and the additional members of the committee for allowing me to testify here today.

Nonpracticing entities or patent trolls have created a new business model that takes advantage of our patent laws in our court system. They have crafted a system of borderline extortion that is a major threat to our economy and jobs. While I am disappointed to hear that the Senate has fumbled the ball in the patent troll litigation reform for this year, I can tell you with full assurance, many of us and my colleague and I in the House will continue to fight this battle until we have won.

While there are many issues in patent troll litigation, each case begins the same, with a recipient of a vaguely worded, highly-threatening demand letter. Unlike other areas of litigation, when it comes to demand letters, things are very out of balance.

One party to the equation asserts a patent infringement with little to no specificity and often is unclear who owns the patent being asserted or how the patent was even allegedly infringed. However, the other party to the equation is typically an honest entrepreneur or business person and must make a decision to either pay the threatening entity to go away or face them in court for extended litigation with an exorbitant price tag attached.

It is time for the entity sending out demand letters, like their community mass mailers, do their due diligence just as we expect in just about every other area of the law. In addition to the amendments I offer on demand letter transparency to the Innovation Act, I have been pleased to work with my colleague across the aisle, Congressman Jared Polis, who is very well addressed in this issue, to address issues throughout the demand letter, the Transparency Act.

This bill would put a lot of specific information about these patent assertion entities and their claims at the fingertips of small companies and retailers who lack the time, money and the resources to respond to the demand letters. We need to require individuals sending an excessive number of demand letters to file information for the U.S. Patent and Trademark Office or the Federal Trade Commission as the chairman's bill would legislate.

We must shine a flashlight on these deceptive fraudulent actors who are operating behind closed doors in the dark. By requiring more transparent litigation practices, we will deter many of the bad actors from being in the litigation abuse business completely, and if that should happen, I would say, good riddance.

Mr. Chairman, while demand letters constitute just one piece of the patent troll litigation problem, it is an important part of any patent troll litigation reform effort. While we discuss the various proposals, we must be careful to strike the right balance to ensure that right shareholders are still able to protect their property, while also going far enough to provide real relief for the victims of this litigation abuse. It is time we start standing up for job creators

and innovative businesses and allow them to get back to doing what they do best, growing companies and invigorating our economy.

To close, I would like to share with you a few sample demand letters that might illustrate the abuse practices we are viewing here today. I will just give a couple of examples. We have one letter here that shows that an individual who has their personal computer but happens to send an email, go to local files, get on the Internet, get on a server, get on a printer, get on a digital copier and any other peripheral matters is infringing upon an patent. It is ridiculous.

Another one simply says that in addition to an alleged patent on this person who sent this letter, they are saying that the person being accused of the patent violation may induce others to infringe on the patent—may induce others to infringe on the patent.

And then finally, we have a situation where they are saying that to prevent, we want to prevent irreparable harm in the future in absence of injunctive relief. It is just another way of saying, if you don't pay the money now, we are going to tie you up in court so long that we will put you out of business.

Chairman, I have some letters that I want to enter into the record, a letter dated from Ni Wang on January 24, 2014; Farney Daniels of August 1, 2012; Innovative Wireless Solutions, April 10 of 2013; and IsaMai from June 16 to 2013. I thank the committee for allowing us to do this, and I yield back.

[The prepared statement of Mr. Marino follows:]

**Congressman Tom Marino: Testimony Before the House Energy and Commerce
Subcommittee on Commerce, Manufacturing, and Trade**

**Hearing on H.R. , a bill to enhance federal and state enforcement of fraudulent patent
demand letters**

May 22, 2014 - 2123 Rayburn

Good morning. I would like to thank you Chairman Terry, Ranking Member Schakowsky, and the Members of this subcommittee, for allowing me to give my testimony on this important topic. Non-practicing entities, or patent trolls, have created a new business model that takes advantage of our patent laws and our court system. They have crafted a system of borderline extortion that is a major threat to our economy and job. While I am disappointed to hear the Senate has fumbled the ball on patent troll litigation reform for this year, I can tell you with full assurance, many of my colleagues and I in the house will continue to fight this battle until we have won.

While there are many issues in patent troll litigation, each case begins the same: with the receipt of a vaguely worded, highly threatening demand letter. Unlike other areas of litigation, when it comes to demand letters, things are very out of balance. One party to the equation asserts a patent infringement with little to no specificity and often it is unclear who owns the patent being asserted, or how the patent was even allegedly infringed. However, the other party to the equation is typically an honest entrepreneur or businessperson who must make a decision to either pay the threatening entity to go away, or face them in court for extended litigation with an exorbitant price tag attached.

It is time for the entities sending out demand letters like they are community mass mailers, to do their due diligence, just as we expect in just about every other area of the law.

In addition to the amendments I offered on demand letter transparency to the Innovation Act, I have been pleased to work with my colleague across the aisle, Congressman Jared Polis, to address this issue through the *Demand Letter Transparency Act*. This bill would put a lot of specific information about these patent assertion entities and their claims at the fingertips of small companies and retailers who lack the time, money, and resources to respond to the demand letters.

We need to require individuals sending an excessive number of demand letters to file information with the US Patent & Trademark Office, or the Federal Trade Commission, as the Chairman's bill would legislate. We must shine a flashlight on these deceptive, fraudulent actors who are operating behind closed doors in the dark. By requiring more transparent litigation practices, we will deter many of the bad actors from being in the litigation abuse business completely—and if that should happen, I would say “good riddance!”

Mr. Chairman, while demand letters constitute just one piece of the patent troll litigation problem, it is an important part of any patent troll litigation reform effort. While we discuss the various proposals, we must be careful to strike the right balance to ensure that rightsholders are still able to protect their property, while also going far enough to provide real relief for the victims of this litigation abuse. It is time we start standing up for job creators and innovative businesses and allow them to get back to doing what they do best: growing companies and invigorating our economy. To close, I would like to share with you a few sample demand letters

that might illustrate the absurd practice we are reviewing today. (Continue to documents, read and request they be submitted to the record) I yield back.

Mr. TERRY. Thank you. And without objection, those letters will be inserted into the record with your oral statement. So appreciate the two of you being active on this important and delicate issue, and taking the time out of your day to participate in our hearing today. Thank you very much.

Mr. MARINO. You are welcome.

Mr. TERRY. Now, at this time, while our friends, Mr. Polis and Mr. Marino are exiting, I am going to start introducing our next panel.

We have Lois Greisman, Associate Director, Bureau of Consumer Protection at the Federal Trade Commission. We are blessed to have Wendy Morgan, Chief of the Public Protection Division, Office of the Attorney General of Vermont; Adam Mossoff, Professor of Law, George Mason University; Rob Davis, Counsel for Venable on behalf of the Stop Patent Abuse Now Coalition; we have John Potter, President and co-founder of Application Developers Alliance; and Alex Rogers, Senior Vice President, Legal Counsel for Qualcomm.

Some of you have been before us in the past and know how these things work. Each of you will have 5 minutes. There is a little box there with green, yellow, and red. I would appreciate it that when it hits the yellow mark that you jump to your conclusions so we can stay on time. And then at the conclusion of the statements, we will go into questions, if we are not on the floor voting at that time.

So at this time, would recognize the gentlelady from the FTC, Lois Greisman. You have your 5 minutes. Will you turn your microphone on. I forgot to mention that part. And we have to have them a little closer, as well.

STATEMENTS OF LOIS GREISMAN, ASSOCIATE DIRECTOR, BUREAU OF CONSUMER PROTECTION, ON BEHALF OF FEDERAL TRADE COMMISSION; WENDY MORGAN, CHIEF OF THE PUBLIC PROTECTION DIVISION, OFFICE OF THE ATTORNEY GENERAL OF VERMONT; ADAM MOSSOFF, PROFESSOR OF LAW, GEORGE MASON UNIVERSITY; ROBERT DAVIS, COUNSEL, VENABLE LLP, ON BEHALF OF STOP PATENT ABUSE NOW COALITION; JON POTTER, PRESIDENT AND CO-FOUNDER, APPLICATION DEVELOPERS ALLIANCE; AND ALEX ROGERS, SENIOR VICE PRESIDENT AND LEGAL COUNSEL, QUALCOMM

STATEMENT OF LOIS GREISMAN

Ms. GREISMAN. Congressman, can you hear me?

Mr. TERRY. We can hear you now.

Ms. GREISMAN. Good. Good morning, again, Chairman Terry, Ranking Member Sarbanes. I am delighted to be here this morning on the behalf of the Federal Trade Commission. I very much appreciate the opportunity to present the Commission's testimony. As you know, my oral remarks are my own, as are any responses to questions you may have, not those of the Commission or any individual commissioner.

I appreciate the subcommittee's sustained interest in the activities of PAEs and the related issues of patent demand letters. Clearly, this is an area of keen interest across the business community

as well as among Federal and State law enforcement agencies. Further, the Commission shares the subcommittee's goal of stopping deceptive demand letters without intruding on the right of patent holders to assert legitimate claims.

As you know, the Commission continues to examine PAEs and demand letters from the policy perspective. The Commission's testimony and my remarks, however, focus on patent demand letters from the angle of consumer protection law enforcement. Briefly, the Commission's Section 5 authority to prevent unfair and deceptive acts and practices can and should be brought to bear with respect to demand letters when appropriate.

While our analysis always will be fact specific, Section 5 may be violated, for example, if a PAE asserts a patent claim where it has no ownership interest or a standing to assert the claim; where the patent or the relevant statute of limitations has expired; where the patent would be covered by an existing license; or where the patent, on its face, relates to a topic obviously unrelated to the claim of infringement.

Further, the PAE also may violate Section 5 where it makes false or deceptive claims that are unrelated to the merit of its patent such as false threats of litigation. On this last point, a ready analogy exists in past cases the Commission has brought dealing with potentially deceptive representations made in connection with attempts to collect a debt. The debt collection actions, some of which preceded passage in 1977 of the Fair Debt Collections Practices Act included a number of cases involving false threats of legal action.

Briefly, these cases hold that a false threat that legal action will be taken, or that legal action will be taken imminently may violate Section 5. Indeed, the FDCPA itself prohibits false threats of legal action in connection with the collection of a debt. Thus, in addition to decisions under the FTC Act, there exists a robust body of FDCPA law, Federal case law that addresses false threats of litigation and false threats of imminent litigation.

It is important to reemphasize that the assertion of a patent claim in and of itself, of course, is not deceptive, and it serves the important purpose of protecting patent rights. Still, the distress experienced by businesses that receive demand letters is real as are the challenges to that business in evaluating how to proceed after the receipt of a demand letter.

It is equally important to keep sight of the fact that concerns about demand letters do not get at the deeper and highly complex issues that underline many businesses' grievances with respect to the patent demands. These critical issues are related to the broad scope of many patents, the ease with which patent infringement claims can be asserted and the cost of defending against such claims, of which some businesses report are simply prohibitive.

Thus, while the current bill provides the Commission with civil penalty authority that it does not currently have, and we believe that civil penalties authority in this area is of potential benefit and may well deter some bad actors. Such new authority does not reach these broader, more fundamental issues.

Additionally, and as outlined in the Commission's testimony, we do have some concerns about the draft's inclusion of a bad faith scienter requirement and its possible application outside the civil

penalty context. At the same time, we do appreciate the bill's inclusion of a savings clause that preserves the Commission's existing authority.

In sum, the Commission's goal is to stop deceptive patent demand letters while respecting the rights of patent holders to assert legitimate claims. We are happy to work with the subcommittee to strike the right balance on this very important consumer protection issue. Thank you.

Mr. TERRY. Thank you, and you have, and we thank you for your effort and help on this matter.

[The prepared statement of Ms. Greisman follows:]

**PREPARED STATEMENT OF
THE FEDERAL TRADE COMMISSION
on
Discussion Draft of Patent Demand Letter Legislation
Before the
SUBCOMMITTEE ON COMMERCE, MANUFACTURING, AND TRADE
of the
COMMITTEE ON ENERGY AND COMMERCE
UNITED STATES HOUSE OF REPRESENTATIVES**

Washington, D.C.

May 22, 2014

I. Introduction

Chairman Terry, Ranking Member Schakowsky, and members of the Subcommittee, I am Lois Greisman, Associate Director of the Division of Marketing Practices at the Federal Trade Commission (“FTC” or “Commission”).¹ I appreciate the opportunity to present the Commission’s testimony on consumer protection issues involving patent demand letters, patent assertion entities (“PAEs”),² and the draft bill.

The activities of PAEs and the related issue of patent demand letters have been topics of increasing interest and concern. Last June, the Executive Office of the President reported that “suits brought by PAEs have tripled in just the last two years, rising from 29 percent of all infringement suits to 62 percent of all infringement suits,” and that this activity may have “a negative impact on innovation and economic growth.”³

The Commission is examining PAEs and patent demand letters from both a policy and an enforcement perspective. This testimony will focus on the latter, and how the draft bill might affect our enforcement efforts.

It is important to note that information about PAEs, how they operate, and their overall impact is limited, and that PAE activity may include a number of different business models.⁴ PAEs could act as efficient middlemen who increase return on investment, particularly for small and individual inventors. PAEs may also have incentives to exploit flaws in the patent system,

¹ This written statement presents the views of the Federal Trade Commission. My oral statements and responses to questions are my own and do not necessarily reflect the views of the Commission or of any Commissioner.

² By patent assertion entities, or PAEs, the Commission refers to firms with a business model based primarily on the purchase and assertion of patents, *i.e.*, firms that seek to generate revenue by licensing, or litigating against, persons who are already using the patented technology.

³ Exec. Office of the President, Patent Assertion and U.S. Innovation at 1-2 (2013), *available at* http://www.whitehouse.gov/sites/default/files/docs/patent_report.pdf.

⁴ GAO, Intellectual Property: Assessing Factors That Affect Patent Litigation Could Help Improve Patent Quality (Aug. 22, 2013), *available at* <http://www.gao.gov/assets/660/657103.pdf>.

generating a harmful tax on innovation. In September 2013, following a joint workshop with the Antitrust Division of the Department of Justice to explore the claimed harms and efficiencies of PAE activity, the FTC announced it would conduct a study to shed light on the practices of PAEs beyond litigation activity and help assess the competitive impact of PAE activity. The FTC is proceeding with this study.⁵

II. FTC Enforcement Authority and Patent Demand Letters

Concerns with patent demand letters, the subject of the draft bill, have emerged with the growth in PAE litigation activity. Although the assertion of a patent claim in itself is of course not deceptive and serves the important purpose of protecting patent rights, the Commission has followed the hearings in this Committee and others that have discussed concerns relating to certain patent demand letters. For example, letters may be sent very broadly and without prior investigation, may assert vague claims of infringement, and may be designed to obtain payments that are based more on the costs of defending litigation than on the merit of the patent claims. Commission staff have heard from businesses and their representatives that believe they have been inappropriately targeted by demand letters. And our staff have actively solicited samples of these letters to determine whether the Commission's authority over unfair or deceptive acts or practices in or affecting commerce, pursuant to Section 5 of the FTC Act, can be used to address them.

We believe that the Commission's Section 5 authority can and should be brought to bear with respect to demand letters where appropriate, as I will discuss more fully below. However, even if its authority is enhanced, the FTC will not be in a position to address the broader and complex issues that underlie many businesses' grievances regarding patent demands. These

⁵ Fed. Trade Comm'n, Notice and Request for Public Comment on PAE Activity, 79 Fed. Reg. 28,715 (May 19, 2013), *available at* <http://www.gpo.gov/fdsys/pkg/FR-2014-05-19/pdf/2014-11484.pdf>.

issues include the broad scope of many patents, the ease with which patent infringement claims can be asserted, and the cost of defending against such claims, which some businesses report as prohibitive. The Commission understands that Congress is seeking to address broader reforms to the patent system and litigation abuses in separate bills.

Although there are limits to the FTC's ability to address concerns with demand letters, the Commission can take action against unfair or deceptive conduct.⁶ Section 5(a) of the FTC Act, the Commission's main operative statute, prohibits unfair or deceptive acts or practices in or affecting commerce.⁷ A company acts deceptively if it makes materially misleading statements or omissions. A company engages in unfair acts or practices if its conduct causes or is likely to cause substantial injury to consumers that is neither reasonably avoidable by consumers nor outweighed by countervailing benefits to consumers or to competition. The Commission can obtain permanent injunctive relief and equitable monetary relief, among other remedies, in appropriate Section 5(a) cases, but cannot obtain civil penalties for violations of Section 5(a) itself.⁸

Depending on the facts, a PAE may violate Section 5 if it asserts a patent claim in circumstances where the PAE has no ownership interest in or standing to assert the patent; where the patent or the relevant statute of limitations has expired; where the patent claim would be covered by an existing license; or where the patent on its face relates to a topic obviously unrelated to the claim of infringement. A PAE also may violate Section 5 where it makes false or deceptive claims that are unrelated to the merit of its patent claims, such as false threats of

⁶ While this testimony focuses on the FTC's consumer protection authority, the Commission is also prepared to exercise its competition authority where warranted.

⁷ 15 U.S.C. § 45(a). The Commission also enforces numerous specific statutes.

⁸ The Commission can seek penalties for some other types of violations, including violations of Commission rules respecting unfair or deceptive acts or practices.

litigation.

The Commission has substantial experience in dealing with potentially deceptive representations made in connection with attempts to collect a debt, which is similar to the patent demand context in that, in both circumstances, individuals or businesses are seeking payments to which they may be legally entitled. Although some FTC defendants have argued that, if their claim for payment is legitimate, they cannot have violated the FTC Act, both the Commission and the federal courts have rejected the argument that a company may lawfully deceive a business or individual who owes, or may owe, compensation to that company.⁹

For more than fifty years, the Commission has pursued deceptive representations made in connection with an attempt to collect an allegedly owed payment. The Commission's enforcement actions have taken place both in the context of debt collection¹⁰ and in a variety of sales contexts.¹¹ These actions have included a number of cases involving false threats of legal action. Decisions in these actions have held that a false threat that legal action will be taken,¹² or that legal action will be taken imminently,¹³ may violate Section 5.

In 1977, Congress enacted the Fair Debt Collection Practices Act ("FDCPA"), which also prohibits false threats of legal action in connection with the collection of a debt. 15 U.S.C. § 1692e(5). Thus, in addition to the decisions under the FTC Act, there is a robust body of FDCPA federal case law addressing false threats of litigation and false threats of imminent

⁹ *In re Trans World Accounts, Inc.*, 90 F.T.C. 350, 399 n.7 (1977), *aff'd in relevant part*, 594 F.2d 212 (9th Cir. 1979); *Floersheim v. FTC*, 411 F.2d 874, 878 (9th Cir. 1969).

¹⁰ *E.g.*, *In re Capax*, 91 F.T.C. 1048 (1978) (debt collector); *Trans World Accounts*, 90 F.T.C. 350 (debt collector); *In re Dean S. Slough*, 70 F.T.C. 1318, 1365 (1966) (seller of debt collection letters), *aff'd*, 396 F.2d 870 (5th Cir. 1968).

¹¹ *E.g.*, *FTC v. Magazine Solutions, LLC*, No. 07-692 (W.D. Pa. Dec. 1, 2008) (magazines); *In re Sunshine Art Studios, Inc.*, 81 F.T.C. 836 (1972) (greeting cards); *In re Wilson Chem. Co.*, 64 F.T.C. 168 (1964) (salve); *In re Wm. H. Wise Co.*, 53 F.T.C. 408 (1956) (books).

¹² *E.g.*, *In re Wilson Chem. Co., Inc.*, 64 F.T.C. at 185; *In re Capax, Inc.*, 91 F.T.C. at 1104 & n.27.

¹³ *E.g.*, *In re Trans World Accounts, Inc.*, 90 F.T.C. at 397-98.

litigation.¹⁴

This enforcement experience and jurisprudence inform the way the FTC approaches potential violations of Section 5 concerning patent demands. As this Subcommittee is aware, FTC investigations are generally non-public, and the Commission does not disclose information such as the identities or alleged practices of individuals or entities under investigation. On January 13, 2014, however, MPHJ Technology Investments, LLC, a company under investigation, sued the Commission, challenging the FTC's authority to take enforcement action against it and seeking an injunction against any law enforcement efforts the agency might pursue.¹⁵ As a result, the Commission can address certain facts that MPHJ has made public through its lawsuit.

MPHJ filed, along with its complaint against the Commission, a draft of a proposed complaint that FTC staff sent to MPHJ's counsel for purposes of settlement discussions. FTC staff's draft complaint alleges that MPHJ had sent letters to thousands of small businesses located in all fifty states representing that the recipient is likely infringing certain patents by using ordinary office equipment. According to the draft complaint, these letters state that the recipients likely need to obtain a license for use of the patents at a price of either \$1,000 or \$1,200 per employee. The draft complaint further alleges that MPHJ's letters represented that substantial numbers of businesses had purchased patent licenses from MPHJ when that was not in fact the case, and that MPHJ's letters also falsely threatened imminent litigation. The Commission has moved to dismiss MPHJ's lawsuit contesting the FTC's authority in this area.

¹⁴ E.g., *United States v. Nat'l Fin. Servs.*, 98 F.3d 131, 138 (4th Cir. 1996); *Crossley v. Lieberman*, 868 F.2d 566, 571 (3d Cir. 1989); *Jeter v. Credit Bureau*, 760 F.2d 1168, 1175–77 (11th Cir. 1985).

¹⁵ *MPHJ Tech. Investments, LLC v. FTC*, No. 14-11 (W.D. Tex.).

III. The Committee's Draft Bill

The Commission shares this Subcommittee's goal of stopping deceptive patent demand letters while respecting the right of patent holders to assert legitimate claims, and recognizes that achieving this goal is not easy. Although the Commission has had only limited time to consider the Committee's draft bill, there are a few observations we can share.

Despite limits on the FTC's ability to address some of the broader issues underlying the issue of patent demand letters, the Commission believes that civil penalty authority in this area is of potential benefit and may deter some bad actors.¹⁶ We appreciate that the draft bill seeks to give the FTC this authority. We note that the new scienter requirement to establish "bad faith" that the Commission would need to meet in order to obtain the civil penalties is consistent with that which already is required to obtain civil penalties under Section 5(m) of the FTC Act.¹⁷ As such, the new scienter requirement is unlikely to create new obstacles for Commission action in the context of civil penalty cases. However, because the FTC Act generally imposes no scienter requirement in non-civil penalty cases (for example, where the Commission seeks injunctive and other equitable relief), this requirement in the draft bill may present hurdles that do not exist under the FTC Act for these matters. Given these potential challenges, among other reasons, the Commission is pleased that the draft contains a "savings clause" that preserves the Commission's existing authority to seek relief other than civil penalties under its existing Section 5 authority.

¹⁶ As noted *supra* footnote 8, the Commission can currently seek civil penalties for violations of Commission rules, such as the Telemarketing Sales Rule and the Franchise Rule, and for violations of certain statutes, such as the Fair Debt Collection Practices Act.

¹⁷ 15 U.S.C. § 45(m)(1)(A).

IV. Conclusion

Thank you for this opportunity to share the Commission's views. We look forward to working with you on this important issue.

Mr. TERRY. Ms. Morgan, you are now recognized for 5 minutes.

STATEMENT OF WENDY MORGAN

Ms. MORGAN. Thank you, Chairman Terry, Ranking Member Sarbanes, and subcommittee members. Thank you for this opportunity to appear before you to give you the perspective of the Vermont Attorney General's Office into your discussion draft. I am glad that the witnesses that have gone before me have laid out the general problems relating to this area because, thinking that I was the last witness, my focus is really much more in the weeds as with regards to your draft.

You asked if there were ways that the draft might be improved to further balance the need to prevent the bad actors from abusing the patent demand letter process while preserving the legitimate purpose of communicating intellectual property rights. That balance is critically important here. I would suggest that there are three ways in which your draft might be improved, all of which would increase the likelihood that the States will take action under any statute that you enact.

There are additional points in my written testimony, which I hope you will consider as well, but I would like to just focus on three this morning. Those will be with regards to the preemptions section; the definition of bad faith, which was already briefly discussed by Ms. Greisman; and also the provision for State action and the jurisdiction for State action.

So as you know from the written testimony, we would prefer that there is no preemption at all within this statute. But if there is, at a minimum, the State laws that exist now should be maintained. But if they are not to be maintained, we would ask that you include a review of your Section 4(a)1. In that section, your general preemption section, you say that the Act preempts any law, rule or regulation, and you also say requirements standard or other provision having the force and effect of law which expressly relates to the transmission or contents of communications relating to the assertion of patent rights.

The difficulty we have with this section is that if we go to court under our Consumer Protection Act, or under our UDAP in other States, the Unfair and Deceptive Acts and Practices Act, then the court will be articulating a standard relating to the transmission or contents of communications, and therefore, at least arguably, we would be preempted under 4(a)1.

So we would suggest that you both eliminate the requirement standard language that is contained in (a)1 to avoid that possibility, and also in the savings clause in (a)2, that you add language that would be comparable to this; that these States may proceed including actions relating to transmissions or contents of communications relating to assertions of patent rights.

In other words, it may be that the preemption statute, as you have it here, would not preempt the State from proceeding under the Consumer Protection Act. But it would be far safer for the States if you were completely clear about that, and the statute as it is here is not clear about that.

With regards to bad faith, our concern is that the current draft requires actual knowledge or knowledge fairly implied that the in-

formation in the demand letter is false. States under their Consumer Protection Acts and UDAP laws do not have to prove knowledge, and that is a very important distinction. If we have to prove knowledge, we are not going to be able to in many instances, and therefore, will be much less likely to proceed under your statute.

Similarly, if even with the language of knowledge fairly implied, again, that requires that it be a false statement and it will not always be a false statement. The people that you are trying to address, the bad actors here are going to change their behavior to meet your statute, and so they will not include false statements. They will include misleading or deceptive statements. So we would recommend that you change the definition of bad faith to be false, misleading or deceptive.

Finally, my third recommendation with regards to the jurisdiction under which the States would bring an action, we would ask that you make it very clear that these are not under patent law, but rather under the Section 5 of the FTC Act, because otherwise, we will end up in a situation where we have the risk of having any decision in district court appealed to the Federal circuit rather than the regional circuit, and the Federal circuit is not used to engaging in UDAP analysis. Thank you.

Mr. TERRY. Thank you.

[The prepared statement of Ms. Morgan follows:]

WILLIAM H. SORRELL
ATTORNEY GENERAL

SUSANNE YOUNG
DEPUTY ATTORNEY GENERAL

WILLIAM E. GRIFFIN
CHIEF ASST. ATTORNEY GENERAL



TEL: (802) 828-3171
FAX: (802) 828-2154

STATE OF VERMONT
OFFICE OF THE ATTORNEY GENERAL
109 STATE STREET
MONTPELIER
05609-1001

**Testimony of Vermont Assistant Attorney General Wendy Morgan
Before the United States House of Representatives
Committee on Energy and Commerce
Subcommittee on Commerce, Manufacturing, and Trade
May 22, 2014**

Summary

Chairman Terry, Ranking Member Schakowsky, and members of the Subcommittee, thank you for the opportunity to testify today. The Vermont Attorney General's Office has been actively working to address the issue of unfair and deceptive communications made in the context of patent assertion and licensing. My office appreciates the work of Congress, and of this subcommittee in particular, in proactively addressing this issue, and we appreciate having the opportunity to share our thoughts on your draft legislation ("Discussion Draft").

State attorneys general are often the first government officials to receive complaints from small businesses and nonprofits that have received vague, confusing, and misleading patent demand letters. We appreciate the subcommittee's efforts to address the issue of troublesome patent demand letters, as part of much-needed broader reforms regarding patent assertion entities generally. My office's experience with these issues informs my testimony with respect to the Discussion Draft. My testimony is summarized below:

- Sections 2(a)(2) and (3) would both benefit from catch-all provisions, and the savings clauses in Sections 3(c) and 4(a)(2) that preserve the authority of the FTC and state attorneys general are critical. Although the practices specified in Section 2(a)(1)-(3) are some examples of the unfair and deceptive practices that my office has observed, once legislation is enacted, bad actors will likely adapt their behavior to avoid practices that are specifically prohibited. However, they may continue to engage in different unfair and deceptive acts. Our recommendations would provide needed flexibility to the FTC and state attorneys general to bring actions under state and federal law to address other practices that may develop in the future that are also unfair and deceptive.
- In order to allow greater flexibility for state enforcement, and consistent with most consumer protection law, state enforcement of any potential legislation should permit the state to act to protect the public interest generally and not limit the state to acting as *parens patriae* for particular residents or require the state to demonstrate that residents have been adversely affected.
- The rebuttable presumption in Section 2(b) seems unnecessary and could create confusion. This could be removed. If it does remain as a rebuttable presumption, the presumption should clearly be limited to compliance with Section 2(a)(4), to avoid any possible misinterpretation that it applies generally to claims of unfairness and deception.
- The definition of “bad faith” should encompass any of the representations set forth in Section 2(a)(2)-(3) that are false, deceptive, or misleading, without respect to the sender’s knowledge. There is traditionally no scienter requirement in consumer protection law. Requiring proof of “actual knowledge or knowledge fairly implied” would create an unnecessarily high bar for an enforcement action and would significantly hinder the ability to enforce the proposed standards for demand letters.
- To prevent ambiguity, it should be clarified that a cause of action under any enacted legislation does not constitute an action arising under the patent laws pursuant to 28 U.S.C. § 1338.
- Limiting the definition of “sender” to a person with a right to license or enforce the patent weakens the ability of the FTC and states to enforce Section 2 against entities that they have no right to license or enforce.
- The definition of “systems integrator” should be broad enough to encompass developments beyond websites and mobile applications that similarly incorporate retail software or services.

Preserving State Enforcement Authority to Fully Protect Consumers

Any federal statute that addresses patent assertion letters should preserve and recognize the full authority of the FTC and state attorneys general to take action against unfair and deceptive communications. The proposed legislation highlights unfair and deceptive practices and promotes increased transparency. Those provisions of the Discussion Draft would provide greater protection to businesses and nonprofits that receive patent assertion letters and will provide them with some of the tools necessary to consider their options. However, there are three areas of the Discussion Draft that my office believes could be clarified or modified to allow states to most effectively protect consumers from unfair and deceptive patent assertion and licensing communications.

First, it is important that the FTC and state attorneys general retain their current authority to protect consumers from unfair and deceptive acts and practices with respect to letters that assert patents and seek licensing fees. Commonly, states are guided in enforcing their consumer protection acts by the FTC Act,¹ but the Act does not generally preempt states' enforcement authority under their own consumer protection statutes.² Federal consumer-protection statutes commonly operate concurrently with state statutory and common law authority.³ We advocate that in the area of unfair and deceptive patent assertion and licensing

¹ See, e.g., 9 V.S.A. § 2453(b); see also Henry N. Butler, *Are State Consumer Protection Acts Really Little-FTC Acts?* 10 (Northwestern University School of Law Scholarly Commons, Faculty Working Papers, 2010) ("Twenty-eight states currently reference the FTC in their CPA.").

² See *Altria Group, Inc. v. Good*, 555 U.S. 70, 91 (2008) (concluding that FTC decisions did not prevent a jury from considering a state deceptive practices claim).

³ See, e.g., Telephone Consumer Protection Act, 47 U.S.C. § 227(g)(6) ("Nothing contained in this subsection shall be construed to prohibit an authorized State official from proceeding in State court on the basis of an alleged violation of any general civil or criminal statute of such State."); Real Estate Settlement Procedures Act, 12 U.S.C. § 2616 ("This chapter does not annul, alter, or affect, or exempt any person subject to the provisions of this chapter from complying with the laws of any State with respect to settlement practices, except to the extent that those laws

communications, federal law act as a floor and not preempt state legislative or regulatory authority, or exempt state laws already in effect as is the case in the Fair Credit Reporting Act.⁴ Vermont, along with nine other states,⁵ has passed legislation that respects the rights of patent holders while protecting consumers and end users who are targeted with deceptive, misleading, and unfair patent demand letters. In our view, these state laws are targeted only at bad actors and do not interfere with the important rights of patent holders to assert their patents honestly and in good faith.

While we prefer that any federal legislation not preempt state laws directed at patent demand letters, we understand that some patent holders object to these targeted state laws and the Discussion Draft would preempt those laws. If the Committee takes this approach, the preemption language should be carefully and narrowly crafted to preserve state authority to enforce consumer protection statutes, including any judicial interpretation of such statutes,

are inconsistent with any provision of this chapter, and then only to the extent of the inconsistency.”); Truth in Lending Act, *Williams v. First Gov’t Mortgage & Investors Corp.*, 176 F.3d 497, 500 (D.C. Cir. 1999) (finding that TILA did not preempt the District of Columbia Consumer Protection Act “and that TILA compliance does not immunize lenders . . . against CPPA [D.C. Consumer Protection Procedures Act] liability.”); Telemarketing and Consumer Fraud and Abuse Prevention Act, 15 U.S.C. § 6103(f)(1) (“Nothing contained in this section shall prohibit an authorized State official from proceeding in State court on the basis of an alleged violation of any civil or criminal statute of such state.”); Fair Debt Collection Practices Act, 15 U.S.C. § 1692n (“This subchapter does not annul, alter, or affect, or exempt any person subject to the provisions of this subchapter from complying with the laws of any State with respect to debt collection practices, except to the extent that those laws are inconsistent with any provision of this subchapter, and then only to the extent of the inconsistency. For purposes of this section, a State law is not inconsistent with this subchapter if the protection such law affords any consumer is greater than the protection provided by this subchapter.”).

⁴ See, e.g., 15 U.S.C. § 1781t(2) (“. . . this paragraph shall not apply with respect to subsection (a) or (c)(1) of section 2480e of title 9, Vermont Statutes Annotated (as in effect on the date of enactment of the Consumer Credit Reporting Reform Act of 1996)”).

⁵ Georgia, Act 809, 2013-2014 Leg., Reg. Sess. (Ga. 2014); Idaho, S.B. 1354, 62nd Leg., 2nd Reg. Sess. (Id. 2014); Maine S.P. 654, 126th Leg., 2nd Reg. Sess. (Me. 2014); Oregon, S.B. 1540, 77th Leg., Reg. Sess. (Or. 2014); South Dakota, S.J. 143, 2014 Leg., Reg. Sess. (S.D. 2014); Tennessee H.B. 2117, 108th Leg., Reg. Sess. (Tenn. 2014); Utah, H.B. 117, Gen. Sess. (Utah 2014); Virginia, S.B. 150, 2014 Leg., Reg. Sess. (Va. 2014) (passed but not signed); Wisconsin, Act 339, 2013-2014 Leg., Reg. Sess. (Wis. 2014).

against unfair and deceptive patent-assertion conduct. If the proposed legislation contains preemption language – which we oppose – the preemption clause should be clearly limited to state laws and regulations that expressly regulate patent-assertion communications, and additional language should be added to clarify that state attorneys general may use existing consumer protection laws to take action against unfair and deceptive patent communications.

Although the list set forth in Section 2(a)(1)-(3) is a relatively comprehensive summary of the unfair and deceptive acts that the my office has observed to date, we expect that bad actors will tailor their communications to comply with these standards but will not stop engaging in unfair and deceptive practices designed to persuade small businesses and nonprofits to pay licensing fees. For example, a communication may state that the patent holder is requesting a licensing fee of \$10,000 based on the price that it has negotiated with others who were similarly situated to the recipient. If, in fact, the patent holder *had* received licensing fees from some individuals who were similarly situated to the recipient, but such licensing fees had never exceeded \$1,000, my office would argue that the statement in the letter was deceptive. However, it would not violate the requirements in the Discussion Draft. This example demonstrates the reality that it is impossible to fully anticipate the unfair and deceptive acts that individuals may engage in. Preserving the authority for the states and the FTC to protect small businesses and nonprofits, end-users of products that they have already paid for, from unfair and deceptive attempts to extort licensing fees will not encroach upon the rights of patent holders who are straightforward and honest in their enforcement efforts. It will, however, provide flexibility for enforcement agencies to address new unfair and deceptive practices that may arise.

Second, as is typically the case in consumer protection causes of action, states should not have to step into the shoes of consumers or show actual consumer harm to enforce the

provisions of Section 2. In enforcing consumer protection laws, my office acts on behalf of the State of Vermont, not any individual citizens. Therefore, unlike a private cause of action for unfair and deceptive practices, which requires the plaintiff to show injury,⁶ a claim brought by a state or the FTC does not typically require a showing of harm.⁷ The states' authority, particularly in this context, would be significantly inhibited if it is limited in this manner.⁸ Requiring states to show that residents have been adversely affected by unfair and deceptive patent assertions or licensing communications would require states to identify consumer harm. This may be particularly difficult when an attorney general's office has received a complaint but has no knowledge of whether the recipient has been sued or hired an attorney to assist in deciding how to respond. Often, the harm of an unfair or deceptive act is likely to occur in the future. Requiring proof of harm to individual consumers will prevent states from acting swiftly to *prevent* the actual harm or injury. My office would recommend that the enforcement authority granted to attorneys general under this act be consistent with typical enforcement authority and not require that the attorney general act as *parens patriae* and prove that recipients have been adversely affected.

⁶ See, e.g., 9 V.S.A. § 2461(b); Cal. Civ. Code § 1780(a); Fla. Stat. § 501.211(s); Mass. Gen. Laws Ch. 93A, § 9; N.Y. Gen. Bus. Law § 349(h).

⁷ See, e.g., *Carter v. Gugliuzzi*, 716 A.2d 17, 23 (Vt. 1998) ("Deception is measured by an objective standard, looking to whether the representation or omission had the 'capacity or tendency to deceive' a reasonable consumer; actual injury need not be shown."); *In the Matter of Daniel Chapter One*, 2009 WL 4086836, *23 n.13 (F.T.C. 2009) ("the FTC need not prove actual injury to consumers").

⁸ Federal statutes take differing approaches to concurrent state authority, some simply provide for state enforcement, while others limit states to acting in the role of *parens patriae*. Compare 47 U.S.C. § 227(g)(1) (granting states the authority to bring a civil action when a person "has engaged or is engaging in a pattern or practice of telephone calls or other transmissions to residents of that State in violation of this section . . ." without the requirement of showing that the interests of residents have been adversely affected) with 15 U.S.C. § 6103(a) (providing authority to bring a civil action as *parens patriae* when it has reason to believe "the interests of the residents of that State have been or are being threatened or adversely affected" by a person engaging in a telemarketing practice in violations of the FTC's rule).

Third, the rebuttable presumption in Section 2(b) is unnecessary, but, if left in, could be clarified to confirm its purpose of protecting businesses acting in good faith that inadvertently send communications with a technical omission of the requirements of Section 2(a)(4). Section 2(a)(4)'s disclosure requirements provide adequate flexibility to protect patent holders that have limited information.⁹ To the extent concerns exist that a technical omission of certain disclosures set forth in Section 2(a)(4) could result in liability under this Discussion Draft, providing a very limited rebuttable presumption could address such concerns. However, as currently drafted, it is not clear whether the intent of Section 2(b) is to provide a rebuttable presumption that the patent holder has complied with the requirements set forth in Section 2(a)(4) or that the patent holder has not engaged in any unfair and deceptive act under the FTC Act generally. The latter would be very problematic and undermine the effectiveness of the proposed legislation.

As I discussed above, my office has significant concerns with the possibility that patent holders who seek to deceive small businesses and nonprofits will comply with the requirements set forth in Section 2(a), but nonetheless engage in unfair acts or include deceptive statements in their patent assertion letters. If Section 2(b) were interpreted broadly to create a rebuttable presumption that the patent holder has not engaged in any unfair and deceptive acts, enforcement agencies would face a higher-than-normal burden of proof in prosecuting even blatantly unfair and deceptive practices by such a patent holder.¹⁰ If the rebuttable presumption is removed, or,

⁹ See Section 2(a)(4)(C) & (D) (both limited "to the extent reasonable under the circumstances").

¹⁰ The typical burden of proof in a consumer protection case is a preponderance of the evidence. See, e.g., *Koch v. Greenberg*, 2014 WL 1284492, at *7 (S.D.N.Y. Mar. 31, 2014) (requiring plaintiff to prove elements in consumer protection case by a preponderance of the evidence); *F.T.C. v. Commerce Planet, Inc.*, 878 F. Supp. 2d 1048, 1055 (C.D. Cal. 2012) (finding that the FTC had proven by a preponderance of the evidence that individual was liable for deceptive and unfair marketing in violation of FTC Act); *State v. Hulsey*, 249 P.3d 468 (Kan. App. 2011) (table)

short of that, references to unfair or deceptive acts or practices and to the FTC Act are stricken from Section 2(b), this drafting problem would be eliminated.

Amend “Bad Faith” to be consistent with consumer protection laws

There are many practices employed by certain patent holders that are unfair and deceptive to recipients of patent assertion and licensing communications. These practices include: indiscriminately sending letters to businesses without particularized understanding of the business’s activities; sending letters that are so vague that the recipient cannot discern the patents being asserted, the alleged infringement, or the party making the assertion; and making express statements in the letters that are factually untrue or misleading.

The Discussion Draft makes it unfair and deceptive to send communications that include the representations in Section 2(a)(2)-(3) if the sender knows, or knowledge can be implied, that the representations were false. My office agrees with the general principal of these requirements but, from an enforcement perspective, believes that the requirements of actual falsity and knowledge or implied knowledge of the falsity will create unnecessary challenges to enforcement actions even where the communications are clearly deceptive and misleading.

Bad actors who wish to send unfair and deceptive patent assertion communications will find ways to comply with the delineated requirements in the Discussion Draft. For example, a statement may be deceptive and misleading without being technically “false.” Requiring actual falsity, as the Discussion Draft presently contemplates, may make it difficult to prove a case against a sender who carefully crafts its letters to avoid outright falsehoods. A letter may state

(distinguishing a criminal charge which must be proven beyond a reasonable doubt, the court noted that “a KCPA [consumer protection act] claim must only be proven by a preponderance of the evidence.”); *Poulin v. Ford Motor Co.*, 513 A.2d 1168, 1172 (Vt. 1986) (explaining that while common law fraud requires clear and convincing proof, consumer fraud requires application of the preponderance of the evidence standard).

that the sender is aggressively pursuing all legal remedies to enforce its patents against other persons instead of expressly stating that the sender has filed litigation against other persons. If the sender has, in fact, only sent initial letters, and has not taken and lacks the capacity to take any further steps to enforce the patent, it is a deceptive and misleading statement. Similarly, a sender may state that it is an agent for enforcing the patents and attach a draft complaint listing itself as the plaintiff. This misleads the recipient into believing the sender is, in fact, an owner or exclusive licensee of the patent, even though it was never expressly stated. Therefore, my office would recommend that the definition of bad faith be amended to include representations that are deceptive or misleading in addition to false.¹¹

Additionally, my office would recommend that the definition of “bad faith” not impose a knowledge requirement that states are not typically required to prove.¹² While the FTC Act has a knowledge requirement for the imposition of civil penalties,¹³ a person that violates an FTC rule, even without knowledge, is liable for injury caused to a consumer irrespective of knowledge.¹⁴ Although we believe civil penalties would be appropriate, as is common in most state consumer protection law, if the relief is limited to injunctions and consumer restitution, the knowledge

¹¹ The FTC has clarified that a “deceptive” practice must have “a representation, omission or practice that is likely to mislead the consumer,” be evaluated “from the perspective of a consumer acting reasonably in the circumstances,” and the “representation, omission, or practice must be a ‘material’ one.” See *Matter of Cliffdale Assocs., Inc.*, 103 F.T.C. 110, at *45 (1984). Including representations that are deceptive and misleading in the definition of “bad faith” would be consistent with traditional understandings of deceptive practices.

¹² See Carolyn Carter, *Consumer Protection in the States*, 17 (National Consumer Law Center) (Feb. 2009) (“Most states do not require the state agency to prove the business’s intent or knowledge.”).

¹³ See 15 U.S.C. § 45(m)(1)(A).

¹⁴ See 15 U.S.C. § 57b; see also *A Brief Overview of the Federal Trade Commission’s Investigative and Law Enforcement Authority*, Section II(A)(1)(b) (2008), available at <http://www.ftc.gov/about-ftc/what-we-do/enforcement-authority>.

requirement should be eliminated. This would be consistent with both traditional state enforcement authority and the FTC authority relating to such relief.

Other Recommendations

The primary concerns of my office are retaining enforcement authority under Vermont's general prohibition on unfair and deceptive acts and practices in commerce and structuring the prohibitions in the Discussion Draft in a manner that would make enforcement actions under an enacted statute tenable from the perspective of state attorneys general. We also have a limited number of additional suggestions that we believe would provide clarification and would help prevent unnecessary litigation over any enacted legislation.

First, Section 2(a) should include a catch-all provision for communications that otherwise include representations or omissions that are likely to materially mislead reasonable recipients. For many of the same reasons discussed in the my earlier testimony, this provision would provide enforcement authorities with the flexibility necessary to address unfair and deceptive practices, even as they change to technically conform with specific examples in any enacted legislation.

Second, because the cause of action proposed in the Discussion Draft would arise under the FTC Act, it would be helpful to clarify that the cause of action would not arise under the patent jurisdiction statute, 28 U.S.C. § 1338. This clarification would not change any authority of the United States district courts, but would provide clarity regarding the appropriate appellate court.

Third, defining the term "sender" is unnecessary. A sender is any person who sends patent assertion communications. By limiting the definition of sender to a person with the right to enforce or license the patents, a person with no such right who sends a patent assertion letter

that, for example, falsely describes existing litigation, would not violate Section 2(a)(2). The same concern arises under Section 2(a)(3). Additionally, because a “recipient” is defined to include only those consumers, end users, or systems integrators who have “no established business relationship with the sender” the definition suggests that a recipient requires a “sender.” Limiting the definition of sender in this way will, at a minimum, create uncertainty regarding the applicability of any provision in Section 2(a) to individuals who send patent assertion or licensing communications without the authority to enforce or license the patent. The State sees no reason to exclude such persons from the prohibitions in Section 2(a)(2)-(3) or to risk debate and judicial and legal resources over whether a recipient requires a sender who is a legitimate patent enforcer. Consequently, if the definition of “sender” remains, it should be amended to include persons that either state or imply a right to enforce or license a patent.

Finally, my office recognizes that the subcommittee has sought to address the concerns faced by many mobile application and website developers that integrate retail software or services into their products or services and face threatening infringement communications relating to the integrated technology. Protection of these systems integrators is similar to protection of end-users and consumers, as such terms are defined in the Discussion Draft, as they are simply incorporating a third party's retail technology. In light of the fast-changing pace of technology, my office recommends that the subcommittee consider eliminating the limitation of this definition to websites and mobile applications, as it may preclude persons developing future technologies that similarly incorporate retail software or services.

Conclusion

The states, because of their ongoing connection with local businesses and nonprofits, play an important role in protecting against unfair and deceptive patent assertion and licensing

communications. The State of Vermont has fought hard to protect consumers and end-users of retail products from abusive practices and seeks to continue coordinating with other states and the FTC in these efforts. The legislation in the Discussion Draft would provide an additional tool for such efforts, which we support, but we do seek to clarify the existing and ongoing authority of states to utilize their consumer protection statutes to address new and changing unfair and deceptive acts as they arise.

While addressing patent demand letters alone will not resolve all of the issues raised in this field, it is a helpful step toward addressing overall patent demand reform. My office greatly appreciates the work that this subcommittee has done to advance this issue, and I thank you for the opportunity to testify.

Mr. TERRY. And Professor, you are now recognized for 5 minutes.

STATEMENT OF ADAM MOSSOFF

Mr. MOSSOFF. Thank you. Chairman Terry, Ranking Member Sarbanes, and members of the subcommittee, thank you for this opportunity to speak with you today about the draft bill prohibiting false statements and mandating disclosures in demand letters. My name is Adam Mossoff, and I would like to note that I am speaking in my personal capacity as a law professor at George Mason University and not on behalf of my employer or any organizations with which I am affiliated.

The draft bill is directed at bad actors who engage in bad faith communications in asserting patents against alleged infringers. Since the draft bill defines bad faith in terms of deceptive or fraudulent statements in demand letters, it is a laudable effort at addressing bad behavior by some patent owners who act illegitimately.

But the draft bill goes beyond this prohibition. It also mandates specific disclosures in all demand letters sent by all patent owners including those sent by legitimate patent owners who are properly licensing their patented innovation in the marketplace or are properly asserting their patents against real infringers. Unfortunately, as a result, the draft bill raises concerns under the First Amendment, and my testimony will focus on two First Amendment concerns with these mandated disclosures.

First, the mandatory disclosure provisions likely violate the First Amendment's guarantee of the right to free speech in communicating freely and truthfully in the marketplace. The Supreme Court has held that the First Amendment necessarily protects the decision of both what to say and what not to say. As a result, the Supreme Court has consistently invalidated as unconstitutional laws and regulations that compel speech in both commercial and noncommercial activities.

A demand letter serves the function of informing its recipient that it is infringing a property right. Without the threat of a potential lawsuit, infringers would hold out and continue infringing, and thus, patent owners would no longer have a right to their patented innovation as secured to them under Federal law. For this reason, demand letters do not fit the Supreme Court's definition of pure commercial speech, which historically has received less protection under the First Amendment.

Instead, a demand letter identifies a violation of a property right and proposes either a legal process in Federal court or a settlement of this legal claim; thus, a law mandating disclosures and demand letters would be strictly scrutinized under the First Amendment's guarantee of the right to free speech. The court will follow the many cases involving similarly compelled speech, even speech by commercial actors in a commercial context and find these mandates likely to be unconstitutional under the First Amendment.

Second, by burdening the legal process of taking the necessary first steps in enforcing legitimate property rights, the draft bill's mandated disclosures likely violate the right to petition also secured under the First Amendment. Now, the Noerr-Pennington doc-

trine prohibits the use of antitrust law to prevent the exercise of the First Amendment right to seek redress for one's legal rights in court.

The draft bill states that violating this provision constitutes a violation of the antitrust laws and it authorizes the Federal Trade Commission to enforce its mandates. As such, the draft bill directly implicates the Noerr-Pennington doctrine.

Now, courts have generally recognized in a wide variety of cases that the Noerr-Pennington doctrine extends to all activities that are necessarily connected to filing a lawsuit in a courthouse. One such activity includes pre-lawsuit communications to settle a legal claim asserted against a defendant. Courts have thus applied the Noerr-Pennington doctrine to patent demand letters.

In one case in 2006, involving an antitrust challenge to an patent owner who sent over 100,000 demand letters to consumers, the court held that applying the antitrust laws in that case violated the Noerr-Pennington doctrine. Several other Federal Courts have reached similar conclusions in recent years. Thus, the draft bill likely imposes an unconstitutional burden on the right to petition secured to all persons under the First Amendment.

In conclusion, excising the bad actors in the patent system is important and laudable because they undermine the efficient operation of our innovation economy. But we must not forget that it is legitimate patent owners engaging in legitimate licensing and assertion activities who make possible America's innovation economy in the first place, which is the engine of economic growth, new jobs and high standards of living. And this is what is being secured by the First Amendment's protections that are implicated by the mandatory disclosure provisions in the draft bill.

Thank you.

Mr. TERRY. Thank you. You may be the first professor to testify in 5 minutes. Thank you.

[The prepared statement of Mr. Mossoff follows:]

STATEMENT OF
ADAM MOSSOFF
Professor of Law
George Mason University School of Law

BEFORE THE
COMMITTEE ON ENERGY AND COMMERCE
Subcommittee on Commerce, Manufacturing, and Trade

U.S. House of Representatives

“H.R. __, a Bill to Enhance Federal and State
Enforcement of Fraudulent Patent Demand Letters”

MAY 22, 2014

INTRODUCTION

Chairman Terry, Ranking Member Schakowsky, and Members of the Subcommittee:

Thank you for this opportunity to speak with you today about the draft bill prohibiting false statements and mandating disclosures in demand letters sent to alleged patent infringers.

The draft bill is directed at bad actors who engage in “bad faith communications” in asserting a patent against an alleged infringer. These communications are identified as “demand letters,” and they are a long-established norm in the innovation industries as a common first step to entering into a license agreement, filing a patent infringement lawsuit, or sometimes both. Importantly, there is no single, clear definition of what constitutes a “demand letter” (a similar situation to the equally ill-defined term, “patent troll,” that dominates the broader patent policy debates).¹ A classic example, though, is correspondence asserting that the recipient is infringing a patent and demanding payment of damages, a royalty for ongoing use, or both.

This bill has laudable provisions aimed at preventing bad actors from strategically exploiting demand letter practices solely to obtain nuisance settlements. Such bad actors have no real

¹ See Hearing on Demand Letters and Consumer Protection: Examining Deceptive Practices by Patent Assertion Entities, Senate Committee on Commerce, Science, and Transportation, Subcommittee on Consumer Protection, Product Safety, and Insurance (Nov. 7, 2013) (Prepared Testimony of Adam Mossoff), at 3-5 (discussing the various usages of this term and how it encompasses both legitimate and illegitimate behaviors by patent owners), available at http://www.commerce.senate.gov/public/?a=Files.Serve&File_id=c5cc328a-af61-4f12-bca7-e2a60fb42ce3; Adam Mossoff, *Thomas Edison was a “Patent Troll”* SLATE (May 19, 2014), at http://www.slate.com/articles/technology/history_of_innovation/2014/05/thomas_edison_charles_goodyear_and_elias_howe_jr_were_patent_trolls.single.html.

interest or legal basis for going to court to obtain legitimate compensation for patent infringement, and the prohibitions in Section 2 on false or deceptive statements in demand letters thus reflect sound industry practices in the legitimate licensing and assertion of patent rights.² Moreover, false or deceptive statements in this context are rightly excluded from well-established First Amendment protections for the right to free speech.³

Yet I am concerned that overbroad legislation could sweep within its prohibitive effects legitimate licensing or assertion activities by equally legitimate patent owners. Other provisions of this bill mandating specific disclosures in demand letters and authorizing the Federal Trade Commission (FTC) to sanction violations of these disclosure requirements are troubling.⁴ In particular, they likely run afoul of constitutional protections long accorded to these communications under the First Amendment.

My testimony will focus on two First Amendment concerns with the provisions of the draft bill that mandate specific disclosures in demand letters. First, these provisions likely violate the First Amendment's longstanding guarantee of the right to free speech in communicating freely and truthfully in the marketplace. Second, by burdening the legal process of taking the first steps in enforcing legitimate property rights, these mandated disclosures likely violate the right to petition secured under the First Amendment. Although bad actors should be excised from the patent system, Congress should tread carefully in considering a bill that threatens to sweep within its prohibitions and sanctions the reasonable licensing and assertion activities of legitimate patent owners.

DEMAND LETTERS ARE PROTECTED SPEECH UNDER THE FIRST AMENDMENT

Some people assume that since demand letters could result in financial remuneration for patent owners, they are a type of commercial speech that may be heavily regulated pursuant to the First Amendment doctrines formulated by the Supreme Court.⁵ This assumption is deeply mistaken. In its "compelled speech" jurisprudence under the First Amendment, the Supreme Court has historically distinguished the strength of the constitutional protection afforded to speech on the basis of whether it is noncommercial or commercial speech.⁶ There is some question as to

² Although the bill defines as an "unfair or deceptive" trade practice within the jurisdiction of the Federal Trade Commission to sanction only statements made in "bad faith," § 2(a)(2)-(3), it expressly defines "bad faith" in terms of actual or constructive knowledge that "such representations were false." § 5(1).

³ See *Central Hudson Gas & Elec. Corp. v. Pub. Serv. Comm'n of New York*, 447 U.S. 557, 593 (1980) ("The Court similarly has recognized that false and misleading commercial speech is not entitled to any First Amendment protection.").

⁴ See § 2(a)(4).

⁵ See *Zauderer v. Office of Disciplinary Counsel of Supreme Court of Ohio*, 471 U.S. 626, 651 (1985) ("[W]e hold that an advertiser's rights are adequately protected as long as disclosure requirements are reasonably related to the State's interest in preventing deception of consumers.").

⁶ Compare *West Virginia State Bd. of Ed. v. Barnette*, 319 U.S. 624 (1943) (applying a type of strict scrutiny in reviewing a state law compelling noncommercial speech) with *Central Hudson Gas & Elec. Corp. v. Pub. Serv. Comm'n of New York*, 447 U.S. 557 (1980) (applying intermediate scrutiny and developing multi-factor test for commercial speech) and *Zauderer v. Office of Disciplinary Counsel of Supreme Court of Ohio*, 471 U.S. 626 (1985) (applying rational basis standard of review for purely commercial speech).

whether this distinction is still viable today, as the Supreme Court has become more solicitous of providing strong protections for commercial speech in recent cases.⁷ But even if the distinction between commercial and noncommercial speech in the Supreme Court's historical precedents were applied to the draft bill, it would still be scrutinized under a stricter constitutional standard of review and it would likely be found wanting.

A demand letter is not commercial speech because its primary function is to inform its recipient that it is infringing a property right secured under federal law. While such a communication has commercial implications, a *legal notice* is not the same thing as an *advertisement* in the marketplace. A demand letter, even if requesting payment of a royalty under a license agreement, is a critical first step to enforcing a *property right*. Without the threat of a potential lawsuit, infringers would "hold out" and continue infringing, and thus patent owners would no longer have a *right* to the patented innovation as secured to them under federal law and pursuant to the Framers' authorization to Congress in the Constitution.⁸

Also, characterizing demand letters as commercial speech conflicts with the essential nature of the American patent system. Patent rights are not commercial monopolies; to the contrary, the longstanding and unique American approach to promoting technological innovation has been to define and secure property rights in innovation.⁹ As such, the claim in a demand letter asserting patent infringement is at heart a legal claim, not a commercial claim. While protecting property, especially patented innovation licensed or sold in the marketplace, has commercial implications, this does not mean that the legal act of securing this property right constitutes an act of commercial speech. In fact, the Supreme Court has repeatedly stated that an *economic motivation* for sending a communication does not by itself define it as a form of commercial speech.¹⁰

For this reason, demand letters do not fit the Supreme Court's definition of commercial speech. The Supreme Court has defined commercial speech as "speech which does 'no more than propose a commercial transaction.'"¹¹ This clearly covers the commercial speech example of an advertisement in the marketplace, but unlike an advertisement a demand letter identifies a violation of a *property right* and proposes either a legal process initiated in a federal court or a

It should be noted that, despite these technical differences in how the speech is reviewed by the Court, in all three of these cases (*Barnette*, *Central Hudson*, and *Zauderer*), the state law was invalidated as an unconstitutional violation of the First Amendment right to free speech.

⁷ See *Sorrell v. IMS Health Inc.*, 131 S. Ct. 2653 (2011) (invalidating Vermont law restricting sale, disclosure, and use of records that revealed the prescribing practices of doctors as unconstitutional compelled speech under the First Amendment); cf. *Citizens United v. Federal Elections Comm'n*, 558 U.S. 310 (2010) (holding that the corporate status of a speaker does not justify suppression of political speech).

⁸ See U.S. CONST. art. I, § 8, cl. 8.

⁹ For a discussion of the constitutional and statutory protection of the property rights in innovation in the American patent system, see Adam Mossoff, *Patents as Constitutional Private Property: The Historical Protection of Patents under the Takings Clause*, 87 B.U. L. REV. 689 (2007); Adam Mossoff, *Who Cares What Thomas Jefferson Thought About Patents? Reevaluating the Patent "Privilege" in Historical Context*, 92 CORNELL L. REV. 953 (2007).

¹⁰ See *Bolger v. Youngs Drug Products Corp.*, 463 U.S. 60, 67 (1983) ("[T]he fact that Youngs has an economic motivation for mailing the pamphlets would clearly be insufficient by itself to turn the materials into commercial speech."); see also *Riley v. National Federation of the Blind of North Carolina*, 487 U.S. 781, 795 (1988) ("It is not clear that a professional's speech is necessarily commercial whenever it relates to that person's financial motivation for speaking.")

¹¹ *Virginia State Bd. of Pharmacy v. Virginia Citizens Consumer Council, Inc.*, 425 U.S. 748, 762 (1976).

settlement of this legal claim. Accordingly, mandated disclosures in demand letters would be strictly scrutinized under the First Amendment's guarantee of the right to free speech, and like other cases involving compelled speech, they would likely be found to be constitutionally suspect.

Even if demand letters are deemed to have a mixture of both noncommercial (legal) and commercial elements, the result would be the same because the Supreme Court has held that mixed speech cases are accorded the more stringent free speech protection given the close constitutional question. As the Court explained in *Riley v. National Federation of the Blind of North Carolina*,¹² when noncommercial and commercial speech are "inextricably intertwined" in a single communication, the communication should be treated for First Amendment purposes as if it is entirely noncommercial speech.¹³ This is the situation with demand letters par excellence. If a demand letter is not deemed to be a pure legal (noncommercial) expression, then a claim to legal protection of a property right against infringement with a concomitant demand for past damages or a future license is still speech that has both non-commercial and commercial elements that are "inextricably intertwined."

The Supreme Court has confirmed the significance of this fundamental insight by consistently and repeatedly invalidating laws compelling speech in a commercial context as a violation of the First Amendment.¹⁴ In such situations, the Court has refused to apply by rote its traditional "rational basis" test for commercial regulations, and it has knowingly departed from this lax constitutional standard even when the speech expressly refers to a product sold in the marketplace.¹⁵ This explains why, despite the ostensibly lax constitutional protection for commercial speech, the Court has trended toward a de facto rule of strict protection for free speech for all types of communications and speakers, both commercial and noncommercial.¹⁶

As applied to demand letters, the Court's compelled speech jurisprudence raises First Amendment concerns about the draft bill's mandatory disclosure requirements. These concerns are rooted in strong constitutional case law in which the Supreme Court has held that "the First Amendment guarantees 'freedom of speech,' a term necessarily comprising the decision of both what to say and what *not* to say."¹⁷ Although constitutional law sometimes can be murky, the application of the "compelled speech" jurisprudence to demand letters is a case in which the Constitution speaks clearly about the protection it affords to patent owners.

¹² 487 U.S. 781 (1988).

¹³ *Id.* at 796 ("[W]here, as here, the component parts of a single speech are inextricably intertwined, we cannot parcel out the speech, applying one test to one phrase and another test to another phrase. Such an endeavor would be both artificial and impractical. Therefore, we apply our test for fully protected expression.").

¹⁴ See *Sorrell v. IMS Health Inc.*, 131 S. Ct. 2653 (2011) (invalidating Vermont law restricting sale, disclosure, and use of medical records as unconstitutional compelled speech under the First Amendment); *Riley v. National Federation of the Blind of North Carolina*, 487 U.S. 781 (1988) (invalidating law compelling speech of professional charity organizers); *Bolger v. Youngs Drug Products Corp.*, 463 U.S. 60, 67 (1983) (holding that an economic motivation for sending a communication does not by itself define it as a form of commercial speech); *Virginia State Bd. of Pharmacy v. Virginia Citizens Consumer Council, Inc.*, 425 U.S. 748 (1976) (holding that a state may not suppress commercial speech regarding lawful activity and concededly true information even when it merely proposes a transaction).

¹⁵ *Bolger v. Youngs Drug Products Corp.*, 463 U.S. 60, 67 (1983).

¹⁶ See *supra* note 7 and accompanying text.

¹⁷ *Riley*, 487 U.S. at 796-97.

DEMAND LETTERS ARE NECESSARILY INCIDENTAL TO THE FIRST AMENDMENT RIGHT TO PETITION

The recognition of the essential legal nature of demand letters as protected free speech raises another equally important First Amendment issue for legislation mandating disclosures in demand letters: “the right of the people . . . to petition the Government for a redress of grievances.”¹⁸ In what is now known as the *Noerr-Pennington* doctrine, the Supreme Court has held that antitrust law cannot be used as a cudgel by which persons are precluded from exercising their constitutionally guaranteed right to seek protection of their legal rights in the courts.¹⁹ Since the draft bill defines any violation of its provisions as an “unfair or deceptive act”²⁰ and expressly grants authority to the FTC to enforce its provisions,²¹ it directly implicates this important constitutional doctrine at the intersection of antitrust law and the First Amendment.

As a preliminary matter, it is important to recognize that courts do not narrowly apply the *Noerr-Pennington* doctrine to cover only specific court filings, such as complaints, motions to dismiss, motions for summary judgment, etc. Instead, the *Noerr-Pennington* doctrine has been extended to protect “conduct incidental to the prosecution of the suit,” such as a “decision to accept or reject an offer of settlement.”²² This makes sense, because limiting the *Noerr-Pennington* doctrine to only the specific legal documents filed in federal court would permit strategic behavior by private and public antitrust plaintiffs seeking to sanction pre-litigation conduct, thereby achieving a *de facto* suppression of a core constitutional right.²³ Thus, as one federal court recognized, “prelitigation activities . . . are protected by the *Noerr-Pennington* doctrine, . . . [which] protects a party’s entitlement to act in furtherance of the First Amendment right to petition governmental authorities for redress.”²⁴

Unlike with the first issue of whether the mandated disclosures in the draft bill fall within the scope of protections for the right to free speech, assessing whether the *Noerr-Pennington* doctrine applies to demand letters does not require making an inference from prior case law. As a judicial doctrine, there is some variance among the courts in how far they have been willing to extend the *Noerr-Pennington* doctrine, but, in recent years, some federal courts have repeatedly held that sanctioning demand letters under the antitrust laws runs afoul of the *Noerr-Pennington* doctrine.

¹⁸ U.S. Const. amend. I.

¹⁹ See *Eastern Railroad Presidents Conference v. Noerr Motor Freight, Inc.*, 365 U.S. 127 (1961); *United Mine Workers v. Pennington*, 381 U.S. 657 (1965).

²⁰ § 2(a).

²¹ See § 3.

²² *Columbia Pictures Industries, Inc. v. Professional Real Estate Investors, Inc.*, 944 F.2d 1525, 1528 (9th Cir. 1991); cf. *Noerr*, 365 U.S. at 143-44.

²³ This corresponds to the exact concerns and impetus for the draft bill currently under consideration by this committee; to wit, limiting the *Noerr-Pennington* doctrine to only court pleadings raises similar concerns about permitting unacceptable strategic behavior given that other bills revising patent litigation practices, such as H.R. 3309, apply only to conduct undertaken after a formal complaint has been filed in court.

²⁴ *DirecTV, Inc. v. Lewis*, 2005 WL 1006030, at *5-6 (W.D.N.Y. Apr. 29, 2005) (citing cases).

In one case involving an antitrust challenge to a patent owner sending over 100,000 demand letters to consumers, the court recognized that “restrictions on presuit demand letters may therefore raise substantial Petition Clause issues if, on examination, such restrictions could impair the right of access to the courts protected by the First Amendment.”²⁵ The court concluded that applying the antitrust laws against the patent owner in this case violated the *Noerr-Pennington* doctrine given “the intimate relationship between presuit settlement demands and the actual litigation process.”²⁶ Moreover, the court further held that “demand letters . . . are not ‘the type of commercial activity that has traditionally had its validity determined by’ the generally applicable competition or regulatory laws. To the contrary, they are the type of activity that typically arises only in the context of contemplated petitioning activity.”²⁷ Several other federal courts have reached similar conclusions.²⁸

The consistent application of the *Noerr-Pennington* doctrine in shielding legitimate demand letters from antitrust scrutiny is directly relevant to understanding the constitutional concerns about the mandated disclosure provisions in the draft bill. Since the mandated disclosure provisions are separate from the prohibition on false and misleading claims, the mandated disclosure requirements bring within the scope of federal antitrust scrutiny *all* demand letters sent by *all* patent owners. This is important for two reasons. First, the mandated disclosure requirements do not fall within the “sham litigation” exception to the *Noerr-Pennington* doctrine,²⁹ because the mandated disclosures necessarily apply to legitimate demand letters sent by patent owners seeking to enforce their legitimate patent rights. Second, as a logical corollary of this first point, the draft bill likely imposes an unconstitutional burden on the right to petition secured to all persons (corporate or natural) under the First Amendment.

THE FUNCTION OF PROPERTY RIGHTS IN INNOVATION

In addition to these fundamental constitutional concerns with the draft bill, there are important policy concerns that counsel against adopting disclosure requirements that necessarily affect all legitimate licensing or asserting of patented innovation. The significance of freely alienable and

²⁵ *Sosa v. DirecTV, Inc.*, 437 F.3d 923, 936 (9th Cir. 2006).

²⁶ *Id.*

²⁷ *Id.* (quoting *Allied Tube & Conduit Co. v. Indian Head, Co.*, 486 U.S. 492, 505 (1988)).

²⁸ See, e.g., *Globetrotter Software, Inc. v. Elan Computer Grp., Inc.*, 362 F.3d 1367 (Fed. Cir. 2004) (holding that *Noerr-Pennington* shields pre-lawsuit communications such as demand letters from both state and federal competition laws); *In re Innovatio IP Ventures, LLC Patent Litig.*, 921 F. Supp. 2d 903 (N.D. Ill. 2013) (same); *DirecTV, Inc. v. Lewis*, 2005 WL 1006030 (W.D.N.Y. Apr. 29, 2005) (holding that *Noerr-Pennington* shields pre-lawsuit communications such as demand letters from federal antitrust law).

Similar conclusions have been reached by courts outside of patent litigation. See, e.g., *McGuire Oil Co. v. Mapco, Inc.*, 958 F.2d 1552 (11th Cir. 1992) (holding that *Noerr-Pennington* protects threats of litigation under Alabama law); *Columbia Pictures Indus., Inc. v. Professional Real Estate Investors, Inc.*, 944 F.2d 1525 (9th Cir. 1991) (applying *Noerr-Pennington* to settlement offer in copyright infringement case), *aff’d*, 508 U.S. 49 (1993); *Barq’s Inc. v. Barq’s Beverages, Inc.*, 677 F.Supp. 449 (E.D. La. 1987) (applying *Noerr-Pennington* protection to presuit threat of trademark infringement); *Coastal States Mktg., Inc. v. Hunt*, 694 F.2d 1358 (5th Cir. 1983) (applying *Noerr-Pennington* to threat of litigation for conversion under state law).

²⁹ See *Professional Real Estate Investors, Inc. v. Columbia Pictures Indus., Inc.*, 508 U.S. 49, 60 (1993). In *Sosa*, the court expressly held that the “sham litigation” exception to the *Noerr-Pennington* doctrine applies if the patent owner engages in misrepresentations or other fraudulent conduct. See *Sosa*, 437 F.3d at 939.

enforceable patent rights, whether in historical context or in today's innovation economy,³⁰ is that this is an essential legal mechanism to bring innovation, such as smartphones, tablets, and personalized medicine, from the lab or garage to the marketplace—and into people's everyday lives. This is what has been achieved by the federal laws and court decisions that comprise the American patent system. It is also indirectly secured by the First Amendment protections implicated by the mandated disclosure requirements in the draft bill.

³⁰ See B. Zorina Khan, *Trolls and Other Patent Inventions: Economic History and the Patent Controversies in the Twenty-First Century*, 21 GEORGE MASON LAW REVIEW 825 (2014), available at <http://www.georgemasonlawreview.org/doc/Khan-Website-Version.pdf>; B. ZORINA KHAN, THE DEMOCRATIZATION OF INVENTION: PATENTS AND COPYRIGHTS IN AMERICAN ECONOMIC DEVELOPMENT, 1790-1920, at 67 (2005) ("Patent laws ensured the security of private property rights in invention and facilitated the development of extensive and deep markets in such rights.").

Mr. TERRY. Mr. Davis, you are now recognized for your 5 minutes.

STATEMENT OF ROBERT DAVIS

Mr. DAVIS. Thank you Chairman Terry, Ranking Member Sarbanes and members of the subcommittee. The SPAN Coalition thanks you for your leadership in addressing patent troll demand letters. SPAN's members include the American Association of Advertising Agencies, the Direct Marketing Association, the Association of National Advertisers, the National Retail Federation and the Mobile Marketing Association.

Whether you are a coffee shop, or retailer or a hotel, an ad agency or any other business or nonprofit, the smash-and-grab tactics embodied in deceptive patent troll demand letters are a scourge affecting main streets across the country. This sad fact was clearly established in the committee's earlier hearings.

Congress can help, and we are extremely pleased that the subcommittee has circulated the discussion draft. We want to commend you and your staff for your excellent work. I was asked to provide SPAN's comments in the discussion draft, and there are seven points. At the outset, I want to flag the definitions of "systems integrator" and "end user."

Given the bill's limitation to only those engaged in the pattern or practice of sending letters, SPAN is concerned that further limiting the scope of the bill to letters sent to end users and systems integrators is not only unnecessary, but also may exclude from the bill's protection certain main street victims of patent troll demand letters. We appreciate the efforts of the staff to get this right. This is a threshold issue for SPAN and we look forward to working with you to resolve it.

Next, SPAN strongly supports the bill's primary objective, which is to clarify the FTC's existing Section 5 authority to bring enforcement actions against those who send unfair or deceptive patent settlement demand letters. The bill targets unfair deceptive practices masquerading as legitimate patent demand letters. As such, addressing this problem is not about patent policy, and it is not about the First Amendment.

Third, we believe the bill fairly well captures the universe of unfair deceptive practices embodied in many of the patent troll demand letters that we have seen. However, SPAN is concerned about other unfair deceptive practices that patent trolls may develop in the future not explicitly included in the discussion draft.

Therefore, we strongly recommend the inclusion of language to clarify that the legislation is not intended to foreclose the FTC's Section 5 enforcement authority to pursue any unfair deceptive acts or practices with respect to patent demand letters not expressly listed in the legislation. SPAN would have grave concerns about legislation that either did not expressly enable such enforcement by the FTC, or would have the effect of foreclosing such future enforcement by the FTC.

Fourth, we believe the bill fairly well captures the basic elements of transparency that should be included in a demand letter. However, we recommend the inclusion of additional elements addressing the settlement demand amount and the basis for it, as well as

further information about real party and interest, all of which we believe would further improve transparency. In addition, we are concerned that certain elements only need to be included to the extent reasonable under the circumstances which would be a loophole that trolls will exploit.

Fifth, the bill seeks to address the concerns of patent holders to send legitimate correspondence by limiting its scope to those who engage in a pattern or practice of sending patent demand letters. SPAN does not oppose such a limitation and concept, provided that it does not get defined in a way that it becomes a loophole easily evaded by trolls.

Similarly, we understand the committee's intent behind including bad faith as an additional condition for certain of the unfair or deceptive practices listed in the discussion draft. SPAN does not necessarily oppose this concept either provided the definition of bad faith is not inconsistent with the FTC's existing standards for unfairness and deception under Section 5, and does not render the law unlikely to be enforced.

Sixth, we are concerned that the bill's inclusion of rebuttable presumption may render the law less likely to be enforced, therefore we recommend that the provision be converted to an affirmative defense.

And seventh, the bill enables State attorneys general to enforce it along with the FTC. However, we believe the State attorneys general ought to be able to seek civil penalties.

At the end of the day, nothing in the bill limits anyone's right to enforce patent, nor does it limit anyone's right to send a demand letter provided the letters are not unfair or deceptive.

On behalf of SPAN, thank you, again, for your leadership in addressing this important issue affecting main street businesses across the country. We fully support your effort, and we look forward to working with the committee as it moves this legislation forward. We hope that the committee can act to complement the work being done on other important forums to address the patent troll problem.

Mr. TERRY. Thank you, Mr. Davis.

[The prepared statement of Mr. Davis follows:]

**Testimony of Robert Davis, Of Counsel, Venable LLP
On Behalf of the Stop Patent Abuse Now (SPAN) Coalition**

**House Energy & Commerce
Subcommittee on Commerce, Manufacturing, and Trade**

**Hearing on “H.R. _____, a bill to enhance federal and state enforcement of
fraudulent patent demand letters.”**

May 22, 2014

Chairman Terry, Ranking Member Schakowsky, and members of the Subcommittee:

On behalf of the SPAN Coalition, I thank you for your leadership in addressing patent troll demand letters. SPAN's members include the American Association of Advertising Agencies (“4A's”), the Direct Marketing Association, the Association of National Advertisers, the National Retail Federation, and the Mobile Marketing Association. But whether you're a coffee shop, a restaurant, a retailer, a marketer, a hotel, an ad agency, or any other business or non-profit, the “smash and grab” tactics embodied in deceptive patent troll demand letters are a scourge affecting main streets across the country. This sad, but incontrovertible, fact clearly was established in the Committee's earlier hearings, both in this Subcommittee and the Oversight & Investigations Subcommittee.

To be clear, we strongly believe innovation is the cornerstone of our nation's economy, but these patent troll practices are not the practices of patent holders legitimately seeking to engage with alleged infringers. As you have heard in previous hearings, for many main street businesses, the receipt of a deliberately vague, unfair or deceptive patent troll demand letter imposes a series of very bad choices for the recipient. Either you hire a patent lawyer to investigate the vague claims in the letter; stop using the technology; ignore the letter at the risk of further harassment and jeopardy; or grudgingly pay the ransom to make the problem go away, which is what the troll is banking on. That's the troll's business model. This all costs main street businesses money they don't have or can ill-afford, especially in this economy, coming at the expense of business expansion and jobs. All the troll needs is a stack of simple form letters, envelopes, and postage stamps.

Congress can help, and we are extremely pleased that the Subcommittee has circulated the Discussion Draft upon which this hearing is focused. I want to commend you and your staff for your excellent work. I was asked to provide SPAN's comments on the Discussion Draft.

While I will discuss this later in my testimony, at the outset I want to flag the definitions of “systems integrator” and “end user,” which we believe exclude from the bill's protections certain main street victims of patent troll demand letters. Therefore, this is a threshold issue for SPAN, and we look forward to working with you to resolve it. That said, the following are SPAN's further comments:

First, SPAN strongly supports the Discussion Draft's primary objective, which is to clarify the Federal Trade Commission's (FTC) existing Section 5 authority to bring enforcement actions against those who send unfair or deceptive patent settlement demand letters. And while the FTC generally has authority to act in this area, we believe it is critically important for Congress to clarify this authority to better protect main street businesses from such unfair or deceptive practices, much like when Congress enacted the Fair Debt Collection Practices Act or CAN-SPAM Act. The Discussion Draft targets unfair or deceptive practices masquerading as legitimate patent demand letters. As such, addressing this problem is not about patent policy, but instead about unfair or deceptive practices. Moreover, we believe this legislation would withstand First Amendment scrutiny.

Second, we believe the Discussion Draft fairly well captures (in section 2(a)) the universe of unfair or deceptive practices embodied in many of the patent troll demand letters that we have seen to date. However, given how these patent trolls are adept in scam artistry, SPAN is concerned about other unfair or deceptive practices that patent trolls may develop in the future, not explicitly included in the Discussion Draft. Therefore, we strongly recommend inclusion of language to clarify that the legislation is not intended to foreclose the FTC's Section 5 enforcement authority to pursue any unfair or deceptive acts or practices with respect to patent demand letters not otherwise expressly listed in the legislation. SPAN would have grave concerns about legislation that either did not expressly enable such future enforcement by the FTC or would have the effect of foreclosing such future enforcement by the FTC.

Third, we believe the Discussion Draft fairly well captures (in section 2(a)(4)) the basic elements of transparency that should be included in a demand letter. However, we recommend the inclusion of additional elements addressing the settlement demand amount and the basis for it, as well as further information about the real party in interest, all of which we believe would further improve transparency beyond the elements in the draft. In addition, we strongly support (in section 2(a)(4)(C) and (D)) requiring an "identification . . . of at least one product, service, or other activity . . . alleged to be infringed" and a "description . . . of how the product service or activity . . . infringes." However, we are concerned that such identification or description is required only "to the extent reasonable under the circumstances." We believe such language could become a loophole that trolls will exploit. We believe that if a patent holder is incapable of such identification and description in a demand letter, then it raises serious questions as to the claims being made in the letter. This is especially so considering that the letters within the scope of this provision would have to be sent within the context of "a pattern or practice" to "end-users" and "systems integrators," and there is a rebuttable presumption that failure to include such information is not an unfair or deceptive practice if a good faith effort is made to include it (and there are otherwise no violations of paragraphs (1) through (3) of subsection (a)).

Fourth, we appreciate the Discussion Draft's focus on fulfilling its primary objective without unreasonably burdening the legitimate correspondence necessary to resolve good faith patent disputes, typically between sophisticated parties, as distinct from the patent troll demand letters besieging main street businesses. SPAN's understanding is that the Discussion Draft seeks to address the concerns of patent holders who send legitimate correspondence by limiting the scope of the bill to those who engage in a "pattern or practice" of sending of patent demand letters. SPAN does not oppose such a limitation in concept, provided that it does not get defined in a way that becomes a loophole easily evaded by patent trolls. Similarly, we understand the

Committee's intent behind including "bad faith" as an additional condition for certain of the unfair or deceptive practices expressly listed in the Discussion Draft. SPAN does not necessarily oppose the concept, provided that the definition of "bad faith" is not inconsistent with the FTC's existing standards for unfairness and deception under Section 5 or does not render the law unlikely to be enforced. We look forward to working with the Committee on this.

Fifth, as previously discussed, the scope of the Discussion Draft to patent demand letters sent to "end users" and "systems integrators." Given the Discussion Draft's limitation to only those who engage in the "pattern or practice" of sending letters, SPAN is concerned that further limiting the scope of the bill to letters sent to "end users" and "systems integrators" is not only unnecessary, but also may exclude from the bill's protections certain main street victims of patent troll demand letters. We appreciate the effort of staff to get this right, and look forward to continuing our work with the Committee in this regard.

Sixth, we are concerned that the Discussion Draft's inclusion of a rebuttable presumption (section 2(b)) may render the law less likely to be enforced. Therefore, rather than a rebuttable presumption, we recommend that the provision be converted to an affirmative defense.

Seventh, consistent with the Discussion Draft, we believe that State Attorneys General ought to be authorized to enforce the federal law, along with the FTC. However, we believe State Attorneys General ought to be able to seek civil penalties, which the Discussion Draft does not permit. We need rigorous State AG enforcement, and the threat of civil penalties are an important deterrent.

At the end of the day, nothing in the Discussion Draft limits anyone's right to enforce a patent, nor does it limit anyone's right to send a patent demand letter, provided - if one is engaged in a "pattern or practice" of sending letters -- the letters contain certain basic information, which legitimate patent holders likely would include anyway, and the letters are not otherwise unfair or deceptive.

On behalf of SPAN, thank you again for your leadership in addressing this important issue affecting main street businesses across the country. Let there be no confusion, we fully support your effort, and we look forward to working with the Committee as it moves this legislation forward.

Mr. TERRY. And now, Mr. Potter, you are now recognized for 5 minutes.

STATEMENT OF JON POTTER

Mr. POTTER. Chairman Terry, Ranking Member Sarbanes, and members of the subcommittee, thank you for shining a light on the deceptive and fraudulent practices of an unseemly new industry. Smash-and-grab patent trolls use shell companies, print-at-home letterhead, and \$0.49 stamps to send baseless patent demand letters that scare small companies, investors and customers, that cause them to pay lawyers instead of hiring new employees and that bully companies into paying extortion settlements simply because they are cheaper than litigation.

I am Jon Potter, and as head of the 2-year-old App Developers Alliance, I have personally spoken with many entrepreneurs and startups that have been shaken down, dispirited and even run out of business by patent trolls. On behalf of our 30,000 members and our 175 corporate members, I am pleased to say that the committee's discussion draft bill is a very good start to a simple antifraud bill.

Despite the background chatter from academics and confused opponents, the committee should rest well, assured that, number one, fraudulent commercial speech is simply not protected by the Constitution; number two, focused legislation to prohibit troll's extortion need not inhibit the honest and fair licensing practices of Qualcomm, Dupont, Gore-Tex, or any legitimate inventor; number three, Congress has previously and successfully required the exchange of basic information in commercial communications where there has been a documented pattern of fraud.

The Fair Debt Collection Practices Act effectively cleaned up an industry that previously was ripe with bullying fraudsters, sort of like patent trolls. Instead of opposing patent reform, legitimate patent owners should welcome congressional action that similarly helps cleanse their industry.

To strengthen the discussion draft, we urge the following important amendments: First, require demand letters to identify specific claims infringed. A single patent often has more than a dozen claims within it. They legally define the borders of the intellectual property. Only the owner who is asserting infringement knows which of those borders have been crossed or infringed upon. It is reasonable, therefore, to require that demand letters include those details, including how each claim was infringed.

Second, require trolls to detail how an infringement is occurring or that they simply don't know but they undertook a substantial investigation to try to find out. The discussion draft requires that demand letters describe infringing activity to the extent reasonable under the circumstances. In the hands of patent trolls, this exception will be abused and the requirements will be ineffectual, unless you also make the troll document that they made a good-faith investigation and that it was fruitless.

Third, protect every business from abusive demand letter fraud. The discussion draft proposes to limit antifraud protection to only some businesses. I know firsthand that often small, creative agencies that build or manage custom Web sites, apps, or software net-

works need protection from trolls. Frankly, all Americans deserve protection from fraud.

Please appreciate a very important distinction. Great American innovators, like Qualcomm, communicate with potential infringers after very careful research. They provide potential licensees with technical and legal background information and documentation. And in good-faith negotiations, they seek legitimate licensing relationships.

In contrast, patent trolls buy cheap patents and use them to extract shake-down royalties from small business. Trolls send ominous and threatening letters but do not include information about how the target's product or technology infringes or which claims are infringed.

Moreover, when targets receive these vague and threatening demand letters and call the troll for more information, they meet stone-faced lawyers who respond with ultimatums: Pay us a settlement or pay lawyers hundreds of thousands of dollars to fight us in court. That is not a choice; that is fraud and extortion.

Some argue that recent increases in patent litigation and demand letters are simply a nuisance byproduct of our innovation economy, a blip on the economic landscape that courts will eventually address so legislation is unnecessary. Others argue that dead-weight loss and failed companies caused by trolls cannot be helped without stepping on the First Amendment or empowering the FTC to be intrusive speech police.

None of this is true. Fraud is squarely within the purview of this committee, and this antifraud bill simply sharpens the FTC's scalpel and aims enforcement resources in the right direction, a direction urged by more than 40 attorneys general and already traveled by 10 state legislators that have enacted demand letter abuse laws.

Yesterday, patent trolls celebrated when the Senate Judiciary Committee announced that small business, tech startups, and main street businesses will endure at least one more year of patent troll abuse. This is disappointing, because comprehensive and effective patent troll abuse legislation is needed. Demand letter reform is an important part of broad reform, but it is also independently important.

On behalf of thousands of innovative App Developers Alliance members, and in support of tens of thousands, if not millions of coffee shops, restaurants, hotels, printers retail stores, banks, credit unions, advertising and marketing agencies, grocery stores, home builders, realtors, and their main street patent coalition, I urge you to quickly legislate standards for a new and growing strain of garden-variety fraud, abusive patent demand letters.

Thank you for your leadership on this important issue. We look forward to working with you to improve and enact this bill.

Mr. TERRY. Thank you, Mr. Potter.

[The prepared statement of Mr. Potter follows:]



Protecting Small and Main Street Business From Patent Trolls' Favorite Bullying Tactic

Summary of Testimony

Jon Potter, President, Application Developers Alliance

Deceptive and fraudulent patent demand letters are harming America's small and Main Street businesses, our tech industry entrepreneurs, and the credibility of our world's-best patent system. Smash-and-grab patent trolls have adopted a business model of sending deceptive demand letters to bully businesses into paying licensing fees or settlements that are often tens of thousands of dollars, and more.

App developers and our Main Street business colleagues urge the Committee to legislate good-faith dealing by all patent owners when they demand licenses and communicate infringement assertions. Legitimate innovators already behave fairly, but trolls do not and so standards must be legislated. The Discussion Draft bill is a strong step in the right direction, but we urge these amendments:

- Demand letters should identify which specific patent claims are allegedly infringed (in addition to identifying the patent).
- Demand letters should document the basis of an infringement assertion, including the result of substantial investigation by the patent owner.
- The bill should not limit protections to only those who use off-the-shelf technology, which excludes creators of custom websites, apps, networks.
- The bill should not limit Federal Trade Commission authority to enforce against deceptive demand letters.

These steps will protect America's innovative startups and our Main Street businesses and restore public trust in our patent system.



Protecting Small and Main Street Business From Patent Trolls' Favorite Bullying Tactic

**Testimony of Jon Potter
President, Application Developers Alliance**

U.S. House of Representatives Committee on Energy and Commerce
Subcommittee on Commerce, Manufacturing and Trade Hearing on:
A Bill to Enhance Federal and State Enforcement of Fraudulent Patent Demand Letters

May 22, 2014

Chairman Terry, Ranking Member Schakowsky and Members of the
Subcommittee:

Thank you for holding this hearing, and for recognizing that deceptive and fraudulent patent demand letters are harming America's small and Main Street businesses, our tech industry entrepreneurs, and the credibility of our world's-best patent system.

In support of our 30,000 individual members, our 175 corporate members, and thousands of businesses represented by our colleagues in the Main Street Patent Coalition, the Application Developers Alliance urges you to swiftly enact legislation to prohibit a favored weapon of America's patent troll bullies – fraudulent demand letters that are intentionally vague, deceptive, and baseless. The Committee's Discussion Draft bill goes a fair distance toward this goal by including modest, common sense standards that require patent assertion letters to simply identify the patent infringed, and how a product or service infringes the patent. And it does so in a manner that promotes the patent system and respects our Constitution.

Substantial research documents nearly \$30 billion dollars of annual economic loss due to patent trolls, and recent studies document incontrovertibly that abusive patent troll litigation is growing. In 2013, the House of Representatives approved legislation to reduce abusive patent litigation – which we hope the Senate will also do very soon. But today the Committee focuses on work left undone in the House bill – eliminating the extraordinary economic damage that happens before litigation, when startups and Main Street businesses are targeted by fraudulent patent troll demand letters. Today's hearing is about legislation that simply will stop fraud: fraud on small business, fraud on the American public, and fraud on the patent system.

Please understand the challenge before the Subcommittee. We are asking you to legislate honesty and good faith dealing by a class of patent owners that thrive and profit on deception, extortion and bad faith – and that rely on our expensive litigation system as their ally and ultimate hammer. These smash-and-grab trolls have adopted a business model of providing minimal information in demand letters, and then refusing to provide additional written or verbal supporting information unless the victimized business spends hundreds of thousands of dollars on lawyers and litigation.

This is not hyperbole. One patent troll sent an Alliance member a 5-page demand letter that included only three sentences describing the patents and the alleged infringement. The remaining 4+ pages threatened “full-scale litigation,” “protracted discovery” and escalating settlement demands if the letter recipient did not quickly agree to a license.

When the company dared to call the troll's lawyer to request more information about the patent, the lawyer refused to respond. He literally answered “no comment” to every question, then asked whether the business was ready to negotiate a

settlement payment, and kindly made a "one-day settlement offer" of only \$50,000. The company was left with only two choices – pay the troll or pay for lawyers. As patent litigation costs average well more than \$1 million, it is foolish for a small business to fight instead of paying the extortion tax.

Neither the App Developers Alliance nor our partners are challenging the patent licensing or enforcement practices of great American innovators like Qualcomm or DuPont. Great American innovators do not license in the manner I have described. Rather, they undertake many hours of research before asserting a patent and demanding a license. They inform the licensee of the basis of their patent demands and provide documentation, including detailed claim charts. They negotiate in good faith and seek win-win solutions and business partnerships. Great American innovators do not say "no comment" and "see you in court" when a potential licensee calls for the first time to ask about the patent and potential infringement.

Demand letters that abuse our patent system are a relatively new phenomenon, but, they are no longer unusual. A survey published by University of California Hastings Law School Professor Robin Feldman in October 2013 documented that fully one-third of startups responding to the survey had received patent demand letters. Sixty percent of those letters came from entities whose primary business is asserting and litigating patents. And when the assertions are deceptive and abusive, and when companies confident that the claim is specious are paying settlements instead of fighting, it is easy to appreciate why demand letter abuse is a growing and successful business model, why more than 40 states' attorneys general are urging federal demand-letter reform and why ten states have new laws prohibiting abusive demand letters.

I urge the Committee to appreciate the extraordinary significance when the government issues patents – in essence awarding valuable monopolies on behalf of all Americans. Patents confer extraordinary power, but should also confer important responsibilities – including honesty and good faith. Patents are similar to government grants, tax exemptions, and contracts. They are all earned and deserved by their recipients, but all come with good faith obligations imposed by Congress.

To ensure that patent owners act in good faith, and have at least a modest basis for asserting that a royalty is due, the Alliance suggests the following amendments to the Discussion Draft:

1. Demand letters should identify which specific patent claims are allegedly infringed, and not only the patent that is infringed. Claims describe each step in the patented technology or methodology and are the core components of a patent. In order to prove infringement the patent owner must prove infringement of specific claims, so it is fair to ask that the patent owner identify in the demand letter which claims have been infringed. This requirement will effectively stop the type of troll that recently sent an Alliance member a four sentence letter asserting that three patents were infringed, but not detailing which of the 58 claims the company had violated.
2. It is not enough that the bill requires a description of the infringing activity “to the extent reasonable under the circumstances.” This is an exception that will swallow the rule as every troll with a mediocre lawyer will exploit it. A demand letter that imposes extraordinary costs and hardships on the recipient should not cavalierly assert infringement without substantial investigation, and the letter should include the results of that investigation.

3. It is critical that the bill protects all victims of demand letter abuse, but the Discussion Draft oddly limits protection to only those who use off-the-shelf technology. Thus, creative agencies that build websites, apps or customized networks are excluded from the bill's protection, and only their clients are protected.
4. Ensure that the bill does not limit Federal Trade Commission authority to enforce against deceptive and unfair practices in any way whatsoever. This bill should clarify and sharpen FTC authority, but should not expand or contract its authority.

Small businesses across all industries – on Main Street, in tech, and in every state and city – face great patent abuse challenges well before litigation when they first receive a fraudulent demand letter. This is because the smallest companies cannot even afford to litigate in federal court, and the mere threat of expensive patent litigation scares off potential customers and investors.

The hardest challenge for the Subcommittee may be to require good faith and fair dealing by extortionist patent trolls without upsetting legitimate enforcement practices of great American innovators. The Discussion Draft makes progress toward threading that needle, but it does not yet effectively protect startups and Main Street businesses from the trolls I have described. Fortunately, the Discussion Draft does not harm legitimate enforcement practices; and it can be improved to strengthen protection against trolls without undermining legitimate patent owners' interests.

On behalf of the millions of small businesses of all kinds represented by the Main Street Patent Coalition, the Application Developers Alliance urges Congress to swiftly enact meaningful requirements for the form and content of demand letters, including a

requirement of honesty and fair dealing, and to pair these requirements with potent penalties for failure to satisfy them. These steps will protect America's innovative startups and our Main Street businesses, and restore public trust in our patent system.

Thank you for your consideration of our views.

Mr. TERRY. Mr. Rogers, you are recognized for 5 minutes.

STATEMENT OF ALEX ROGERS

Mr. ROGERS. Chairman Terry, Congressman McNerney, and members of the subcommittee, thank you for the opportunity to appear today to discuss patent demand letters. My name is Alex Rogers, and I am senior vice president legal counsel for Qualcomm. Qualcomm is a member of the Innovation Alliance, a coalition of research and development-focused companies that believe in the critical importance of maintaining a strong patent system.

Qualcomm is a major innovator in the wireless communications industry and the world's leading supplier of chipsets than enable 3G and 4G devices. Qualcomm's founders are the quintessential example of American inventors in the garage who built one of the world's foremost technology companies. Through ongoing investments in research and development and broad licensing of our patented technologies, Qualcomm has created thousands of well-paying jobs for U.S. workers and helped foster a thriving mobile industry.

It is worth noting that Qualcomm is not a plaintiff in any pending patent litigation, but we are a defendant in numerous patent infringement lawsuits, some of which were brought by so-called patent assertion entities. However, I am not here to criticize or defendant PAEs, but instead to address what we believe should be the proper focus of any patent demand letter legislation; namely, targeting abusive demand letter activities without unintentionally damaging important patent rights.

Notice letters play an important role in the patent system, both for patent holders and accused infringers. Patent law encourages and sometimes requires patent holders to take reasonable steps to notify others of possible infringement. Meaningful patent protection, including the ability to provide notice, is a key factor for companies like Qualcomm in deciding whether to invest in new products and technologies.

Qualcomm appreciates the committee's interest in curtailing abusive demand letter activities; at the same time, we urge the committee to be cautious so as not to inadvertently hinder legitimate patent enforcement practices. A demand letter law that makes patent notification or enforcement too burdensome, too costly or too risky may deter appropriate notice activity and undermine incentives to innovate.

As the committee proceeds with this bill, we believe the following guiding principles will help strike the appropriate balance: First, the bill should clarify rather than expand the FTC's existing authority under Section 5 to address abusive demand letters; second, the bill should be limited to situations in which the sender has engaged in a pattern or practice of mailing bad-faith demand letters to consumers or end users.

The pattern or practice requirement appropriately targets the mass mailing of deceptive demand letters and is consistent with the FTC's Section 5 authority. And explicit bad-faith requirement is necessary to protect patent holders' First Amendment rights. It also avoids punishing patent holders for good-faith conduct. Limiting the bill to communications sent to consumers and end users

protects those most vulnerable to abusive demand letters while reducing the risk that the FTC will be drawn into business-to-business disputes.

Third, the bill should clearly describe the conduct that would be considered unfair and deceptive and not impose overly-burdensome disclosure requirements.

Fourth, the bill should preempt State demand letter laws. Although State enforcement may be appropriate in certain circumstances, it would be extremely burdensome to subject patent owners to disparate and overbroad State demand letter requirements.

Keeping these principles in mind, the draft bill has a number of strengths. For example, the bill focuses on those engaged in the pattern or practice of sending unfair and deceptive demand letters to consumers and end users. The bill sets forth reasonable disclosure requirements and specifically describes the conduct that would be considered unfair and deceptive, and the bill preempts State demand letter laws. We urge the committee to retain these requirements and limitations in the bill.

On the other hand, there are provisions of the discussion draft that require further refinement. For example, the definition of systems integrators is overbroad. Additionally, the discussion draft would cover not only statements made in demand letters but things implied by them. This language could create too much uncertainty with respect to compliance and enforcement.

Qualcomm looks forward to working with the committee in its efforts to achieve a balanced and appropriately tailored bill. Thank you for allowing me to testify today, and I look forward to answering your questions.

Mr. TERRY. Thank you.

[The prepared statement of Mr. Rogers follows:]

Statement of
Alex Rogers
Senior Vice President, Legal Counsel
Qualcomm, Incorporated
Before the
Subcommittee on Commerce, Manufacturing, and Trade
Committee on Energy and Commerce
United States House of Representatives
113th Congress, 2nd Session
May 22, 2014

Introduction

Chairman Terry, Ranking Member Schakowsky and Members of the Subcommittee, thank you for the opportunity to appear today to discuss patent demand letters. My name is Alex Rogers, and I am Senior Vice President, Legal Counsel for Qualcomm, Incorporated. Qualcomm is a member of the Innovation Alliance, a coalition of research and development-focused companies that believe in the critical importance of maintaining a strong patent system that supports innovative enterprises of all sizes.

Qualcomm, Patents and Innovation

Qualcomm's founders are the quintessential example of the storied American "inventors in the garage" who built one of the world's foremost technology companies on the foundation of highly innovative technology and strong patent rights. Since our founding in 1985, Qualcomm has evolved into a leading innovator in the wireless communications industry, and a recognized pioneer in the development of 3G and 4G wireless technology.

Qualcomm designs, has manufactured on its behalf, markets, and sells products and services based on these and other digital communications technologies. Our products consist principally of integrated circuits (also known as chips or chipsets) and system software used in mobile devices and in wireless networks. Seventy percent of our 31,000 employees (65 percent of whom are engineers) are based in the United States. Qualcomm invests about 20% of its annual revenue in research and development. R&D expenditures for the 2013 fiscal year alone totaled approximately \$5 billion. As we develop new technologies, we patent them to protect that investment. In the United States alone, Qualcomm has approximately 12,000 issued patents and approximately 12,000 pending patent applications.

Through ongoing investments in research and development (R&D) and broad licensing of our patented technologies, Qualcomm facilitates billions of dollars in exports, while creating thousands of well-paying jobs for U.S. workers. Moreover, through our R&D investments and licensing program, Qualcomm has helped create a thriving mobile ecosystem. Qualcomm's core wireless technologies are integral to 3G and 4G mobile phones, tablets, e-readers, mobile applications, and a host of other wireless devices and services. Qualcomm is the world's leading supplier of chipsets that enable these 3G and 4G devices.

Qualcomm is not a plaintiff in any currently pending patent litigation. At present, we are a defendant in several patent infringement lawsuits, some of which were brought by so-called patent assertion entities (PAEs) asserting questionable infringement claims and patents of dubious validity. However, the objective of my testimony is neither to criticize nor defend PAEs. Rather, I am here today to testify regarding what Qualcomm believes should be the proper focus of the Committee's legislation—abusive demand letter conduct—and the best way to target such conduct without unintentionally damaging important patent protections.

Qualcomm is pleased to see that the current bill proposed by this Committee has a number of strengths that other proposed measures relating to demand letters do not have. For example, the current bill focuses on those engaged in a pattern or practice of sending unfair and deceptive demand letters to consumers or end users. Additionally, the bill contains reasonable disclosure requirements, specifically sets forth the conduct that would be considered unfair and deceptive, and does not give the Federal Trade Commission discretion to regulate demand letter content. Nonetheless, further changes are required to make sure that the bill is narrowly focused on the bad faith actors that are the cause of the problem and does not contain broad provisions that undermine the appropriate exercise of patent rights.

Notice letters and licensing communications are an important part of the U.S. patent system

A strong patent system, which has its roots in Article 1, Section 8 of the U.S. Constitution, is an essential part of America's economic success, contributing to economic growth, higher income, and more jobs. Strong patent rights incentivize investments in technological innovation. IP-intensive industries account for more than one third of U.S. GDP, and directly or indirectly support approximately 40 million jobs. It is critically important to maintain a strong patent system that promotes innovative enterprises of all sizes.

Notice letters play an important role in the patent system. Indeed, as the Supreme Court has explained, "[p]atents would be of little value if infringers of them could not be notified of the consequences of infringement." *Virtue v. Creamery Package Mfg. Co.*, 227 U.S. 8, 37-38 (1913).

Patent law encourages patent holders to take reasonable steps to notify others of existing or pending patent rights and their possible infringement. In some instances, federal patent law requires patent holders to send notice letters to accused infringers to preserve their patent enforcement rights and ability to collect damages. Notice letters and licensing communications can also serve the interests of accused infringers. Once a patent holder has made its rights known, the accused infringer can determine whether to cease the allegedly infringing activities, negotiate a license, or decide to continue its activities based on an assessment of non-infringement or invalidity. Moreover, knowledge that new products or products in development may practice the patent or patents of another allows potential infringers an opportunity to design around existing intellectual property while still producing a product which is socially and economically beneficial, or even perhaps improve upon the invention or invent an alternative.

Any demand letter legislation must be careful not to discourage legitimate patent-related communications, which are integral to the functioning of the patent system and the resolution of patent disputes, including possible resolution without resorting to litigation.

Abusive demand letters

We have all heard stories of the mass mailing of bad faith patent demand letters by PAEs or “patent trolls” to small businesses, consumers, and technology end users. Through the indiscriminate sending of bad faith demand letters, some bad actors have co-opted and distorted an otherwise legitimate patent enforcement practice in an attempt to extract payment from groups of people who are generally unfamiliar with the patent system.

Qualcomm understands and appreciates the Committee’s interest in curtailing the abusive activities of these bad actors. At the same time, we urge caution and balance to ensure that efforts to address this problem do not inadvertently harm legitimate patent enforcement practices.

Unnecessarily broad legislation will cause unwanted “collateral damage”

A demand letter law that is too broad or too punitive may deter appropriate and useful efforts to provide notice of patent infringement activity and runs the risk of undermining incentives to innovate. The value of a patent rests in the patent holder’s ability to enforce it in a meaningful way. Innovators must assess their ability to enforce and license the intellectual property relating to their inventions when deciding whether to make the significant investments necessary to develop and/or commercialize new products and technologies. The availability of meaningful patent protection is also key to the development of business partnerships and cooperative relationships in key technology areas. Making notification obligations or enforcement of patent rights too burdensome, too costly, or too risky will adversely affect the dynamics of innovation investment. Accordingly, any legislation should target remedying the problem of abusive mass demand letter campaigns, without harming patent holders engaged in legitimate patent enforcement activities.

An effective solution does not require sweeping legislation or an expansion of the FTC’s authority to police the enforcement-related communications of all patent holders. Indeed, the FTC already has the authority to protect consumers from unscrupulous actors who engage in the mass mailing of blatantly unfair or deceptive demand letters. The FTC has begun to take action against such bad actors under its existing authority. A bill that injects the FTC into private disputes over the validity or worth of patents would adversely affect both patent holders and accused infringers. Private disputes and negotiations do not need to be regulated in this manner. The Committee’s bill should clarify, rather than expand, FTC authority.

The Committee’s demand letter legislation should draw a clear line between deceptive shakedown scenarios warranting FTC enforcement and routine individualized patent correspondence between companies, the vast majority of which is legitimate. FTC enforcement authority granted by the bill should be limited to those situations in which the sender has engaged in a pattern or practice of mailing bad faith demand letters to consumers, end users, or

other similarly situated letter recipients likely to lack a familiarity with patent law or the resources necessary to evaluate and respond to a demand letter.

Limiting the bill to communications sent to “consumers” and “end users” furthers the goal of protecting those most vulnerable to abusive demand letters while reducing the risk that the FTC will be drawn into individual disputes between patent owners and potential licensees or alleged infringers. The “pattern or practice” requirement is appropriate because the purported need for demand letter legislation stems from just this kind of activity—the mass mailing of demand letters by patent trolls. The “bad faith” requirement is necessary to capture the requirements of current case law and protect patent holders’ First Amendment rights. These requirements are consistent with the requirements imposed on the FTC by Section 5 of the Federal Trade Commission Act and existing case law. Indeed, limiting the bill to instances in which there is a “pattern or practice” of behavior is not only consistent with the FTC’s Section 5 authority, but similar provisions can also be found in other specific FTC statutes. Inclusion of these requirements will help to strike the correct balance between identifying the situations in which FTC can and should take action, and protecting the rights of patent holders.

Furthermore, if Congress is going to legislate in the area of demand letters, Congress should specifically describe the conduct that would be considered unfair and deceptive. This clarity is necessary to prevent the bill from being misinterpreted and to put patent holders on notice of what type of conduct is prohibited.

Legislation should avoid overly burdensome disclosure requirements

The Committee should avoid imposing overly burdensome disclosure requirements that fail to account for the realities of patent enforcement and licensing negotiations. Not all licensing communications involve a handful of patents and a small number of commercially available accused products. Often, licensing negotiations involve a portfolio of hundreds or thousands of patents and numerous different devices, product models, or manufacturing processes. Some or all of these potentially infringing devices, product models, or processes may not be available to the patent holder. Even assuming such information is readily available to a patent holder, requiring disclosure of highly detailed information in a demand letter (such as an identification of each asserted claim and each accused product model or process, and a detailed explanation of how each claim is infringed) would impose an undue burden on patent owners and could result in voluminous communications. For some patent holders, particularly small inventors, start-ups and those lacking extensive resources to devote to patent enforcement, such a burden would be enormous, expensive and impractical, and could impair their ability to enforce their intellectual property rights.

Legislation should protect good faith conduct and the constitutional rights of patent holders

We ask that the Committee refrain from creating a framework under which a patent holder could be punished for good faith conduct. Indeed, the First Amendment affords broad protection for activities relating to the enforcement and communication of patent rights, and courts have repeatedly held that a patent holder should not be penalized for communicating its patent rights or an allegation of infringement in good faith. Any proposed legislation should be drafted with these concepts in mind.

The real consumer protection threat posed by demand letters results from the sending of bad faith communications to unsophisticated recipients. The appropriate goal of the legislation should be to identify, and empower the FTC to address, only those demand letters that are sent in bad faith.

Federal preemption of state demand letter laws is necessary for clarity and uniformity

Congressional demand letter legislation should preempt state demand letter bills. Patent law has long been the exclusive province of the federal government. However, over the past year, several states have passed legislation relating to patent demand letters. These state bills contain disparate requirements and prescriptions. Ensuring compliance with federal legislation, as well as a patchwork of state laws, will make enforcement of patent rights extremely burdensome and, for some patent holders, prohibitively expensive, which in turn will chill the sending of patent-related communications, even those communications which are entirely legitimate and made in good faith.

Furthermore, some of the recently passed state bills contain provisions that could be subject to abuse by accused infringers. For example, many state bills allow the recipient of a demand letter to pursue a private cause of action against a patent holder and seek tens of thousands of dollars in punitive damages. As a result, patent holders may find themselves the target of private plaintiffs threatening or instituting litigation in order to extract nuisance settlements. Provisions of this nature are likely to incentivize, rather than prevent, vexatious litigation. The federal government is best positioned to address the problem through balanced legislation that will be applied uniformly throughout the nation.

Conclusion

Qualcomm respects the Committee's efforts to find a sensible solution to the problem of abusive demand letters. As noted, the draft bill has a number of strengths. For example, the bill appropriately focuses on those engaged in a pattern or practice of sending unfair and deceptive demand letters. It correctly focuses on letters sent to consumers and end users. The bill sets forth reasonable, but not unduly burdensome, disclosure requirements. It specifically describes

the conduct that would be considered unfair and deceptive, and does not give the FTC discretion to regulate demand letter content. It is critical to retain these requirements and limitations.

There are provisions of the discussion draft that require further honing to ensure that the bill is clear and appropriately focused. For example, at present, the definition of “systems integrator” is overbroad. To the extent the “systems integrator” concept is included in the bill, it should be tailored to cover small businesses that utilize a finished or off-the-shelf software product to develop a website or mobile application for end users, without sweeping in large sophisticated producers of software, websites, or computer applications. Additionally, section 2(a) of the discussion draft covers communications that “imply” infringement on the part of the recipient. This type of vague language creates too much uncertainty with respect to compliance and enforcement.

Qualcomm looks forward to working with the Committee in its efforts to achieve a balanced and narrowly tailored bill. Thank you for allowing me to testify today, and I look forward to answering your questions.

Mr. TERRY. And that concludes the testimony, and we will enter the questions from this panel up here.

And I want to start with you, Mr. Rogers. I guess, last to speak, first to answer questions. You testified that the concept of bad faith is, “necessary to capture the requirements of current case law.” Can you please elaborate a bit on that comment?

Mr. ROGERS. Well, again, it is appropriate in light of what we are trying to target here, and that is bad-faith, abusive behavior, and we want to, as Mr. Chairman said, thread the needle. We want to avoid deterring good-faith patent assertion. The bad-faith requirement also, we believe, is necessary for this bill to survive the challenges that Professor Mossoff has identified. We think it is important and necessary in order to make the bill appropriate and viable under the First Amendment and under the Noerr-Pennington doctrine that Professor Mossoff identified.

Mr. TERRY. Thank you.

Ms. Morgan, in that same respect, you indicated during your testimony that bad faith is problematic and should be taken out. Would that make this law of strict liability such that even if a person innocently misstates something in a letter or a series of letters that they could, in theory, be civilly—that they could be liable for civil penalties?

Ms. MORGAN. I am not saying that you need to eliminate bad faith entirely. I think you need to have some sort of attribute with regards to Sections 2(a)1, 2 and 3 because—I am sorry.

Mr. TERRY. That is all right.

Ms. MORGAN. I am not used to testifying here, needless to say.

Mr. TERRY. We are just talking here, don’t worry. There is no audience.

Ms. MORGAN. Right. So I do think that you need something comparable to your bad-faith requirement or definition, but I think the problem is with the definition that you have here, and that is that it requires knowledge or that people effectively know and you can attribute them to having knowledge.

And both knowledge and falsity, because it is entirely possible that these letters will be particularly going forward, not exactly false, but they may be misleading and deceptive. And so you want to be careful that you don’t eliminate enforcement when you don’t have a false statement or when you cannot prove that the sender had knowledge.

That also relates to, I think, the benefit of having a catch-all clause. I think that if you just list, enumerate things that will violate the Act then you are going to eliminate the possibility of using the Act going forward, because the patent, what people have been calling the patent trolls, those who are sending fraudulent letters at this point in time will change their behavior. And so you need the courts and the FTC and the States to be able to enforce even when they do change their behavior if it is essentially the same kind of deceptive behavior.

Mr. TERRY. OK. Appreciate that.

So Ms. Greisman, I appreciate, again, all of your effort and we will continue to work together on this. You mentioned under Section 5 that you can currently hold someone liable and obtain an injunction against conduct that wasn’t intentional, but is deemed un-

fair and deceptive. And so if we don't include the scienter requirement in this bill, does that mean that you could hold someone liable and obtain civil penalties for conduct that wasn't intentional?

Ms. GREISMAN. No, it does not. Under the Federal Trade Commission Act, in order for the Commission to obtain civil penalties, there exists, by statute, a knowledge requirement which is comparable, largely comparable to the knowledge requirement in the bill which speaks of actual knowledge or knowledge fairly implied. So the Commission already, under current bylaw, has to show some level of knowledge in order to obtain civil penalties. Separate from that, as you note, in order to obtain an injunction or other equitable relief, the Commission does not have to show any knowledge.

Mr. TERRY. OK. I appreciate that.

I am going to yield back my time and recognize the gentleman from Maryland who is the acting ranking.

Mr. SARBANES. Acting ranking. Thank you, Mr. Chairman. I appreciate the opportunity to ask them some questions, and we don't have a lot of time here so let me get right to some of the provisions in the bill because we want to get some of your answers on the record.

Ms. Morgan, your testimony is particularly important because you are, you know, at the State level trying to apply these enforcement opportunities and seek the appropriate remedies, so we want to make sure that in the drafting the bill we don't, in some way, constrain your ability to do that.

You expressed some concern that Section 4(b)1 requires State attorneys general to show actual consumer harm before they bring a case under the bill. And I was curious if that is a requirement that is consistent with typical consumer protection causes of action?

Ms. MORGAN. No, it is not. And there are two parts of that section that are unlike, at least the Vermont statute, and I believe in many other statutes. First of all, we don't have to act as *parens patriae*. We come in as the State. We are not standing in the shoes of the consumers.

And similarly, your bill here requires that we prove that a consumer or an end user has been adversely affected. And what that is going to do is to prevent us from coming in and stopping patent trolling when we first hear of it, if the person who received the letter has not been adversely affected. If they come to us immediately and say look at this letter, can you do something about it, can you stop it from going to other Vermont companies or nonprofits, we wouldn't be able to under this provision. So we would want to come in under our Consumer Protection Act in that case.

Mr. SARBANES. It takes away your ability to be sort of preemptive in the way you are doing some of the enforcement, it sounds like.

The draft also limits remedies available to State attorneys general to injunction and compensatory damages on behalf of recipients who suffered actual harm. And I am wondering, would that limitation of remedies affect your office's likelihood of bringing claims under this statute?

Ms. MORGAN. I think that it would. Under our Consumer Protection Act and UDAP laws in other states, we have the ability to get penalties and the ability to get attorneys' fees and costs, and that

is a very important deterrent to the companies that are issuing these letters.

Mr. SARBANES. Thank you. Also, I would like to note that a recipient under this bill is considered not to have a, quote, established business relationship with the sender, end quote. Are there problems with the way that this language could be interpreted; and if so, how would it affect your office or agency's ability to enforce the law?

Ms. MORGAN. There are problems, and thank you for asking that. Because the definition of sender does not include the fraudulent patent demand—people who are sending fraudulent demand letters. So the definition of sender is really undermining your statute here. There is a violation only if there is a recipient, and recipient has to have a relationship with a sender, at least arguably that is the case. And so, again, we would get into a dispute in court about whether or not this is an actual sender or not under your statute. And frankly, the more you can solve the problems before we get to court, the better off we will all be and the more likely we will bring an—

Mr. SARBANES. So that is definitely another potential constraint.

Mr. Davis, you stated that SPAN would have, I think you said, grave concerns about legislation in this area that did not expressly enable the FTC to reach other unfair or deceptive practices that patent trolls may develop in the future, not explicitly included in the Section 2 of the draft. Can you explain that a little bit more?

Mr. DAVIS. Yes.

Mr. SARBANES. Thank you.

Mr. DAVIS. This relates to the application to the Noerr-Pennington doctrine. There is some, I think, misconceptions about what Noerr-Pennington is. It is a court-created doctrine of statutory interpretation that applies when you have a broad, a statute of broad application like the antitrust laws as Professor Mossoff mentioned, or potentially Section 5 of the FTC Act.

What happens in that case when someone goes after what might be considered petitioning behavior, under these broad statutes, the court will look and ask whether Congress intended that statute to deal with that type of petitioning behavior. If that petitioning behavior isn't specifically mentioned, then the court will read that out of the statute. So even if the broad language of the statute covers that particular conduct, if it is petitioning behavior, it won't be read as covering it.

Mr. SARBANES. OK.

Mr. DAVIS. The courts have actually been split on whether demand letters are petitioning behavior, but seems like there is a movement towards finding that demand letters are petitioning behavior. So there is a concern that if Congress doesn't write this law and include a broad language, a catch-all provision, that the courts will read the statute as limiting the FTC's authority to what is specifically mentioned in the bill under Noerr-Pennington.

Mr. SARBANES. Thank you very much. Yield back.

Mr. TERRY. Thank you. Gentleman from Mississippi is recognized for 5 minutes.

Mr. HARPER. Thank you, Mr. Chairman.

Mr. Davis, you expressed concern that while you supported a threshold, the phrase “pattern or practice” could create a loophole that could easily be evaded by patent trolls. You know, we don’t want that either. Can you give us an example of how it could be evaded?

Mr. DAVIS. Thank you. We actually support the use of pattern and practices as a threshold to the statute. It prevents the use of the statute—or the bill, I am sorry, from being used against legitimate patent holders and we agree with these in that circumstance. It is, however, a threshold. It’s threshold language for all of the substantive provisions in the Act, and we are concerned if the definition of the term is too restrictive, that it will limit the application of the bill unduly.

Mr. HARPER. All right. Ms. Greisman, in determining what a pattern or practice looks like, is there any existing law or rule that on which you could rely, or would rely?

Ms. GREISMAN. I am not aware of any statute or rule enforced by the FTC where that kind of language actually constrains the ability of the agency to act, though that kind of language does appear in private causes of action and I think perhaps some laws enforced by the States.

Where the constraint is is the Commission is authorized by law only to act in the public interest. What that means is it does not act where there are purely private disputes or isolated incidents, so there has to be something that is affecting the marketplace in a significant enough manner to rise to the level of warranting Federal action.

Mr. HARPER. OK. All right. Well, Mr. Davis, hearing Ms. Greisman’s interpretation of the phrase, do you still have concerns about the phrase?

Mr. DAVIS. I don’t. I think, I agree with Ms. Greisman’s discussion. I think that there is still the same concern given the absence of the use of that phrase.

Mr. HARPER. OK.

Mr. DAVIS. But, again, we support use of pattern or practice, assuming that the definition works.

Mr. HARPER. Ms. Greisman, if I could ask you, Mr. Rogers testified that private disputes and negotiations, presumably between large, sophisticated companies, do not need to be regulated. Are there any limiting principles of FTC law rules or enforcement guidance that would preclude the FTC intervening in actions between two such companies?

Ms. GREISMAN. I respectfully go back to my prior comment that the Commission is required to act only in the public interest, and it would not be, in my mind, in the public interest to intervene in what I consider purely private disputes or isolated incidents that do not have a significant impact on the market.

Mr. HARPER. All right. Let me ask you this: The standard in the draft for defining an unfair or deceptive act or practice is to engage in a pattern or practice of sending letters in bad faith that are false or deceptive. The FTC enforces violations of other rules such as we have discussed, Fair Credit Reporting Act, that permits civil penalties for a knowing violation that constitutes a pattern or practice. Have there been any difficulties meeting that standard in FTC en-

forcement cases of FCRA, and is there any reason why this standard could cause problems in that context?

Ms. GREISMAN. I am not aware of any problems in the Fair Credit Reporting Act context, and I would not anticipate at this point any in this context.

Mr. HARPER. All right. Mr. Davis, if I could come back to you on the issue of rebuttable presumption.

Mr. DAVIS. Yes.

Mr. HARPER. You expressed concern that the rebuttable presumption will render this bill less likely to be enforced. A sender of one of these letters can only avail themselves to the rebuttable presumption if they don't engage in any of the prohibitive behavior of subsection A, paragraphs 1 through 3, and they make good faith to disclose what is required under subsection A, paragraph 4.

In other words, if they don't engage in any of the bad behavior, they can't be held liable for a technical violation because the FTC thinks that they didn't do a good enough job with the disclosures. Why would that hinder enforcement against people who made purposely false statements or people who make purposely false statements in conjunction with omissions?

Mr. DAVIS. Well, I agree, Congressman, that the rebuttable presumption only applies to the transparency provisions. But those transparency provisions are very important. The principal problem that we have, that our members have with patent trolls is how expensive it is to deal with those demand letters. That is the force behind the patent troll demand letters.

And the transparency provisions are very important in helping us lower the cost of dealing with those demand letters. The information that you would use to figure out whether there is a good faith effort to come up with the information needed to put in the demand letter relating to how the patent is being infringed by the product or service that the recipient has is in the possession of the sender of the letter.

Mr. HARPER. Got you. OK.

Mr. DAVIS. And as a result, it seems more appropriate for this to be a—rather than a rebuttable presumption, to be an affirmative defense, something that that person sent, no matter what proof.

Mr. HARPER. Thank you, Mr. Davis. And I am past my time. I yield back, Mr. Chairman.

Mr. TERRY. Yes. Thank you. And recognize the gentleman from California.

Mr. MCNERNEY. Thank you, Mr. Chairman. And I thank the witnesses this morning. You know, no piece of legislation is perfect. We are not talking mathematics here. We are taking English, and eventually we have to vote on these things, so I would like to know from each one of you, would you support this if you were a member of Congress and it was up for final vote, starting with Ms. Greisman, yea or nay.

Ms. GREISMAN. That is a tough question.

Mr. MCNERNEY. We have to face these tough questions once in awhile.

Ms. GREISMAN. I think that what the bill does is it provides the Commission with an additional tool that it does not currently have,

which is civil penalty authority, and I think, on balance, that is positive.

Mr. MCNERNEY. OK. That is a yea then. Thank you. Ms. Morgan.

Ms. MORGAN. I appreciate that this is a positive step forward, but I think there are too many problems with it as it is and so that it will not be effective in the way that you would like it to be effective.

Mr. MCNERNEY. So nay. Professor.

Mr. MOSSOFF. I recognize that it is very important not to let the perfect be the enemy of the good, which is always a danger to academics face, and I think the preemption provisions and the prohibitions on false and misleading statements in section 2 are excellent and would do much to address the identified problem with the bad actors, but I would still have constitutional reservations about the mandatory disclosures, and so with that, those reservations, I would probably vote no.

Mr. MCNERNEY. Thank you. Two noes, one yes so far.

Mr. DAVIS. It wasn't the question you asked, but with the amendments that we proposed, we would be in favor of it. As I said in the testimony, the systems integrator definition is a gating—is a gating issue for us.

Mr. MCNERNEY. So yea. Yes, Mr. Potter.

Mr. POTTER. As I said to the chairman when I met with him yesterday, if the door is locked and there are no meal breaks and no bathroom breaks, we can get this to a place where it is a really good bill. In fact, it will be a great bill, but at this point, with the coverage not including substantial numbers of our members who receive, regularly receive demand letters and have been sued and put out of business by trolls, we couldn't support this bill as written, but we look forward to that door is locked and no meal breaks meeting.

Mr. MCNERNEY. Thank you.

Mr. ROGERS. I think there is commonality on the definition of the recipients. The system integrator language has—is not broad enough in certain respects, according to my colleagues, and it is also broad in other respects. It would sweep in very sophisticated large manufacturing companies like cell phone manufacturers and computer manufacturers, and even car companies that are essentially system integrators. Ford would be a system integrator under this, and I think that is unintended. But I think that if we can work on the definition of "recipients," this is a very good, very well-balanced bill that threads that needle between trying to target abuse by bad actors and trying to protect good faith rights activities of patent holders.

Mr. MCNERNEY. So is that a yea or a nay?

Mr. ROGERS. That is a yea with work on the definition of "recipients."

Mr. MCNERNEY. Very good. Professor, do you think it is possible to thread this needle?

Mr. MOSSOFF. With—

Mr. MCNERNEY. To protect patent holders and yet to protect small businesses?

Mr. MOSSOFF. Yes, I think it is completely possible to thread the needle. And in fact, I think the provisions of section 2 that address

what reflects the real concerns, which is the misleading and false and deceptive statements in letters that are being sent out to unsophisticated individuals and small businesses would be properly addressed by that, and in fact, those prohibitions are important, too, because they bring themselves—they bring the statute there for within the exceptions to both the Noerr-Pennington Doctrine under the sham litigation exception as well as the predicate requirement under the First Amendment that there is—under First Amendment analysis that there is no protection for false or misleading or deceptive statements.

Mr. MCNERNEY. Would it be possible to limit the number of letters that a patent assertion entity could send out? Would it be possible to say you can only send out 10 letters or 100 letters or—by the Constitution?

Mr. MOSSOFF. I don't think there is anything in the Constitution that would say you could limit or permit the letters. I do think that as an underlying policy matter, though, it would be very difficult to identify what would be the appropriate number or amount because we just don't know on a going forward basis how new innovative technology would be deployed in the marketplace and potentially used or exploited by legitimate users or infringers. And the whole purpose of the patent system is to, in fact, promote and bring into the hands of consumers that new innovative technology, and we need to make sure that there is this appropriate legal protections provided to the creators of those technologies when they come up with them.

Mr. MCNERNEY. OK. Thank you.

Mr. TERRY. Thank you. The gentlelady from Tennessee is recognized.

Mrs. BLACKBURN. Thank you, Mr. Chairman, and I want to thank each of you for your time and for your patience and working with us through this. I know you are hearing a lot of the section 3, section 5 conversations, and our concerns there. So, Ms. Greisman, let me come to you. Mr. Davis recommended a language change for you-all, that the bill include language to clarify this legislation is not intended to foreclose the FTC section 5 enforcement authority to pursue any unfair deceptive acts or practices with respect to patent demand letters not otherwise expressly listed in the legislation.

So, I am asking you, the savings clause in section 3(c) was meant to accomplish precisely that, so are you concerned—do you have concerns about the language and whether or not there is adequate protection for the existing section 5 authority?

Ms. GREISMAN. Thank you. I appreciate the question. I do think the savings clause as drafted is consistent with other savings clause, and it most likely is adequate to the task.

Mrs. BLACKBURN. You do. OK. Mr. Potter, let me come back to you, if I can. You stated that it is important this bill not, and I am quoting you, limit the Federal Trade Commission's authority to enforce against deceptive and unfair practices in any way whatsoever. But the bill contains an explicit savings clause ensuring that the FTC can still pursue action against trolls under the section 5 authority.

So, are you concerned that the savings clause is not sufficient to preserve the FTC's enforcement authority.

Mr. POTTER. Congresswoman, I made an executive decision in between my written testimony and my oral testimony not to include that point because I am deferring to the Federal Trade Commission on the matter of the savings clause that affects their authority.

Mrs. BLACKBURN. So you are going to work on this?

Mr. POTTER. I am prepared to work on this.

Mrs. BLACKBURN. OK. That sounds great. Ms. Morgan, you are getting a workout today, aren't you? And you have expressed some concern on the preemption provision, that it removes your ability to protect consumers under your laws of general applicability. The intent was to create a single uniform law with respect to patent demand letters but not to remove existing consumer protection angles. Can you describe the language that causes you concern in section 4(a)(2) or provide the committee in a short period of time. You can do this—we are short on time today. You can submit this in writing if you would like.

Give us what you think would be better alternative language, and you suggest clarifying that a clause of action brought under this Act would not arise under, let's see, 28 U.S.C 1338, and I would like for you to explain the effect of this. And you can do all of this in writing because we are short on time, and I want to come to Ms. Greisman for one more footnote 6 of your testimony states that the FTC is prepared to use its competition authority in this context, if warranted. So, I would like for you to expand on that, and I would also like for you to give us what a hypothetical would—

Ms. GREISMAN. Any competition issue, and we obviously do have competition authority under section 5 of the FTC Act.

Mrs. BLACKBURN. Right.

Ms. GREISMAN. And our competition authority does extend to transfers of intellectual property—

Mrs. BLACKBURN. OK.

Ms. GREISMAN [continuing]. Issues that might relate to collusive behavior, monopolization or attempts to monopoly, but the competition inquiry is so highly fact-specific, I really would be hard pressed to provide—

Mrs. BLACKBURN. OK.

Ms. GREISMAN [continuing]. A hypo at this point.

Mrs. BLACKBURN. All right. I will take that as your answer. Mr. Chairman, in the interest of time and votes coming up, I yield back.

Mr. TERRY. Thank you. And recognize the gentleman from Vermont.

Mr. WELCH. Thank you very much, Mr. Chairman. You know, is it within your power to lock this great panel into a room with no bathroom breaks or window in order to come out with that bill we want.

Mr. TERRY. I don't know. We should write a bill.

Mr. WELCH. Well, I want to thank the panel. I especially want to recognize Wendy Morgan who has been a great member of the Attorney General's Office in the State of Vermont for years, and of course, Vermont has been a leader on this. A lot of our small busi-

nesses are just getting hammered, and we have got to do something, bottom line. We just have to do something. It is outrageous when you are a MyWebGrocer or another small company and you are getting these rip-off patent letters.

We had a nonprofit that some parents with disabled kids started, and they scraped together money, bake sales, everything, and they get these rip-off patent letters, so it is a problem. But the fact it is a problem, we don't want to come up with a solution that creates other problems, we get that, but the closed room with no windows, that is no a bad idea because we do have to solve this, and I appreciate your leadership on this, Mr. Chairman.

But let me ask Mr. Rogers and Mr. Potter. You know, the old tech companies that are reputable have valuable patents and they have got to protect them. We get that. And new tech companies are oftentimes on the receiving end of some of these patent trolls, so there is legitimate interest on both sides, and it is legitimate, I understand, for you both to be looking at this from the perspective of the folks you represent. And it is a lot of the small guys in Vermont that are advocating this so vigorously, but we have got IBM, which is the biggest engine of our economy in the state, very important.

Is there a way to draft this that you both are satisfied?

Mr. ROGERS. So, Congressman, I would be happy to answer that first. Absolutely.

Mr. WELCH. Well, I am going ask quite seriously, the suggestion, you can help us on this because I think this panel here wants to do something that solves the problem but doesn't create another one, and you have a collective knowledge and experience, you know what the reality is, but my request of you is that you really do spend some time trying to work out what those differences are. We are not going to do it right here, but I don't know, Mr. Chairman, I mean, that would be helpful to us, wouldn't it, because—

Mr. TERRY. Yes, it would.

Mr. WELCH [continuing]. Our goal is to get a bill that works.

And let me ask, Professor, you want as little intervention as possible, and here is my question. If there is little intervention as possible means the status quo continues and our nonprofits and our small emerging tech companies are getting hammered and harassed and bled to death financially, that is not acceptable, and I wouldn't think it would be for you, so would you see there to be a need to provide some protection against the abuse of the process to protect those folks?

Mr. MOSSOFF. Oh, certainly, and I hope I made it clear that I believe that the prohibitions on sending false and deceptive and misleading letters are acceptable and appropriate, and as a matter of fact, do address, I think, the concerns that had been raised by some of the bad actors in the patent system. I think that the important principle, though, that we always have to remember is that costs are symmetrical, that—and I think you have been touching on this, that—to create systemic changes that address bad actors creates burdens and costs for good actors as well.

Mr. WELCH. Yes, but that is—that is a drafting issue. I mean, to say that, basically, if we say that solving one problem is going to cause another, to me, there are two outcomes. One is you don't

do anything, so then you keep a bad situation continuing for innocent people, or if you fix it, you have really got to thread that needle and do the hard work to find a way where the good actors are protected and the bad actors are hammered.

Mr. MOSSOFF. Right.

Mr. WELCH. Now, Ms. Morgan, on preemption. You know, Vermont, Mr. Chairman, has a very active consumer protection bureau and it has helped small businesses and it has helped a lot of our consumers, so it is important for us in Vermont to maintain that ability for our Attorney General's Office to protect our citizens and our small businesses, and the preemption issue is a big one, and I just want to give you a chance to speak a little bit more about that, Ms. Morgan.

Mr. TERRY. In 19 seconds. No pressure.

Ms. MORGAN. Preemption, preemption, preemption, don't do it.

Mr. TERRY. Got it.

Ms. MORGAN. The States want to protect the small businesses and the nonprofits that are, as you say, getting hammered, and we can do that under our Consumer Protection Act if you don't in some way interfere with that, so my initial testimony was around being sure that you not interfere with it.

And furthermore, if you want us to use this statute, it has to be in a form that is useful and doesn't create a lot of risk of litigation around peripheral issues, so I am all in favor of locking us in a room. I think that is a good idea, and as you, Representative Welch know, I spend a fair amount of time locked in rooms in the Statehouse or in the cafeteria trying to resolve things in precisely that way, and it is an excellent way to go.

Mr. TERRY. Thank you.

Mr. WELCH. I yield back.

Mr. POTTER. Mr. Chairman.

Mr. TERRY. Mr. Kinzinger from Illinois is recognized for 5 minutes.

Mr. POTTER. Mr. Chairman, may I take one moment to answer the question that was asked of me?

Mr. TERRY. Sorry.

Mr. POTTER. OK.

Mr. KINZINGER. Thank you, Mr. Chairman, and again, thank you-all for being here, and I know it is a very important issue and one that has been rightfully getting a lot more of attention lately.

Mr. Rogers, I am going to start with you, and actually, I may basically focus exclusively on you. Today we are trying to tackle the dangers of abusive demand letters. I have heard from restaurant owners in my district that have received these demand letters because they are using credit card machines. So, there is a problem that needs to be addressed. I think that is very obvious. With that said, in your business, what are some legitimate purposes that you think demand letters can serve?

Mr. ROGERS. So, to start with, Congressman, demand letters can avoid litigation. We receive demand letters all the time, and it puts a party on notice that there is a property rights issue that exists with respect to their products, and you can actually deal with a demand letter in a variety of different ways. If you pay attention to it, you may be able to say you are wrong, it doesn't affect our prod-

uct, and let me explain why. You may also decide to enter into a license, and we have done both, and sometimes it results in litigation, and litigation has to move forward.

But the demand letters are a necessary precursor toward resolving property rights, and in the ongoing litigation, if it actually does occur, demand letters actually set markers that matter for purposes of either establishing liability or establishing a right to certain damages. So, demand letter and notification is integral to the patent system that we have.

Mr. KINZINGER. And we have heard from a number of stakeholders that are requesting a general catch-all prohibition on fraudulent statements. You testified that clarity is necessary in this bill to prevent misinterpretation and to put individuals on notice of what conduct is unlawful. Would tying a catch-all to the concept of fraudulent statements made in bad faith as defined in this bill provide acceptable notice?

Mr. ROGERS. I think the problem with the catch-all is that, that it tips the balance between targeting bad faith and bad actors and trying to avoid harming good faith patent holders. It tips the balance too far in the wrong direction. If you have a catch-all, it creates a chilling effect with respect to the companies that want to assert their patent rights in good faith, particularly smaller companies. We are going to be very concerned about what is involved and what that means, and they may feel that they are going to get trapped, and it creates a chilling effect towards asserting their patent rights to begin with, and that, in turn, then creates and tends to undermine their incentives to innovate and get patents in the first instance. So I'm very concerned about a catch-all.

Mr. KINZINGER. So, I have another question, but actually, what I am going to do because I am in a good mood and it is our Friday, kind of, Mr. Potter, if you wanted to respond to the question that was asked of you previous, I will give you little bit of time, because you seem like you were just sitting there wanting to respond, so go ahead.

Mr. POTTER. Thank you very much, Congressman. Let me say in his absence to Congressman Welch and to the subcommittee, I think the answer is yes, that we can reach a resolution, but the resolution must have some basic information required in demand letters, and I don't think Mr. Rogers is even disputing that. And so the professorial First Amendment argument, which has been rejected by courts in the Fair Credit Debt Practices Act—Collection Practices Act, is specious and just needs to be pushed aside, but beyond that, on these practical issues of whether we are protecting billion dollar companies or billion dollar market companies or five-person companies, we can figure out a way to address that issue.

Mr. KINZINGER. Thank you. Mr. Chairman, I yield back.

Mr. TERRY. Thank you. At this time recognize the vice chairman, Mr. Lance.

Mr. LANCE. Thank you very much. Good morning to the panel. Let me say it is my view that Congress are the last people on earth who should suggest that you should be locked in a room to solve the problems of the United States.

To you, Mr. Rogers, I have no doubt that there are frivolous demand letters that are sent, and we should do all that we can to

crack down on this abuse, from my perspective, we also must be careful lest we unintentionally hurt legitimate investors. There is, of course, no patent police, and patent rights are enforced by individuals who hold those patents. My question to you is this, what harm might be done to the economy if we pass legislation that hampers innovators from enforcing their valid patent rights?

Mr. ROGERS. So, the harm to an economy that has transitioned from being primarily a manufacturing economy to an innovation economy—

Mr. LANCE. Yes.

Mr. ROGERS [continuing]. Is very, very significant.

Mr. LANCE. Yes.

Mr. ROGERS. And so threading the needle here is critical, very important, and I think that this step, this bill is very well-balanced. As I said before, we had some things to work on. I would urge you not to do things that undermine small inventors. And just touching on Mr. Potter's last comment, if we ladle into this bill onerous disclosure requirements relating to identifying every claim and every detail of every infringement theory, a prolific small inventor who has a portfolio of 100 or a couple of 100 patents or even scores of patents, will find that to be so daunting and so expensive and so lawyer-intensive, that he is going to wonder why he got his patents to begin with. We have to be very careful, and I think this committee has done a very good job so far of being very careful.

Mr. LANCE. Thank you. Thank you very much, Mr. Rogers. Professor Mossoff, would any of the required disclosure elements in the draft, standing on their own, pass First Amendment analysis? Is this a way to cure—are there any ways to cure the flaw, or are there any disclosure elements that we could require to test such an analysis from your perspective, sir?

Mr. MOSSOFF. Thank you, Congressman, and it is an excellent question. And because of the structure of intermediate test scrutiny sometimes given and the multi-factor test that they developed under the Central Hudson decision, it is difficult to answer the question in the abstract.

Mr. LANCE. Yes.

Mr. MOSSOFF. So, any one particular disclosure requirement, probably in isolation, it would probably be upheld as legitimate. The difficulty and concern, of course, is a slippery slope.

Mr. LANCE. Of course.

Mr. MOSSOFF. And what you see in the Supreme Court's precedents going back 30 years in Bolger and Riley and Zauderer and Central Hudson, going all the way back to the Virginia Board of Pharmacies where the Supreme Court has repeatedly held that even seemingly innocuous disclosure requirements addressing simple facts have been struck—have been struck down as being unconstitutionally compelled speech.

Mr. LANCE. Because of—in part, because of the slippery slope.

Mr. MOSSOFF. Yes, in part because of the slippery slope and that even in the commercial context, yes, speech has economic motivation, but nonetheless, it embraces noneconomic communications, yes, were fact-based but nevertheless themselves are not commercial standing.

Mr. LANCE. And it has been a long time since law school, and Virginia Pharmacy was quite awhile ago, wasn't it?

Mr. MOSSOFF. That was back in the early 1970s, but coming all the way up to Sorrell, 2012, which involved—the Supreme Court struck down the—a Vermont statute or requiring disclosure of pharmaceutical records by prescribing physicians as an unconstitutional compelled speech.

Mr. LANCE. Thank you very much. I yield back the balance of my time, Mr. Chairman.

Mr. TERRY. Recognize the gentleman from Missouri, Mr. Long for 5 minutes.

Mr. LONG. Thank you, Mr. Chairman. And Mr. Davis, you qualified your acceptance of the bad faith concept so long as it is not inconsistent with FTC's existing standards for unfairness and deception. Does it matter that the definition of bad faith in this bill was borrowed from the FTC Act and it is something the FTC must show in order to obtain civil penalties, which is a remedy for the violation to outline in this bill?

Mr. DAVIS. Thank you, Congressman. It does matter and it is important. Our concern is that the language diverges slightly from the language in section 5 of the FTC Act. There is at the very end of the provision, so that the FTC Act relates to actual knowledge or knowledge fairly implied on the basis of objective circumstances that such act is unfair or deceptive; whereas, this bill relates to actual knowledge or knowledge fairly implied on the basis of objective circumstances et cetera because such representations were false. And we are concerned that the—that the bad faith definition implying falsity rather than deceptive would allow patent trolls to slip in literally true but deceptive representations in their demand letters that the FTC would not be able to go after under the current definition.

Mr. LONG. OK. OK. Thank you. And Ms. Greisman, the first thing I want ask you is how many different ways are there to mispronounce your name?

Ms. GREISMAN. Infinite number.

Mr. LONG. You probably heard them all, haven't you?

Ms. GREISMAN. I am sorry?

Mr. LONG. I say you probably heard them all, haven't you, all the different ways, but you indicated that the FTC is familiar with the scienter requirement in the bad faith definition and that you do not anticipate new obstacles in the context of civil penalty cases which can arise under this Act. How do you prove that someone has actual knowledge or knowledge fairly implied?

Ms. GREISMAN. That can be proved in a variety of ways, and I want to just pick—

Mr. LONG. Can you pull your mic just a little bit closer?

Ms. GREISMAN. Sure. Sorry. That can be proved in a variety of ways, and I just want to pick up on something that Mr. Davis said. I agree with everything he said, and I did not think, within the narrow context of civil penalties, our burden is significantly different than it is otherwise by the requirement to prove something is false because of the narrow prohibitions in the statute, in the proposed bill itself. As a general matter, I agree with him that it could be problematic.

Proving actual knowledge can be done any variety of ways. It could be done through deposition testimony, through e-mails, through written correspondence, and the same for knowledge—knowledge fairly implied. It is a burden of proof that we are quite familiar with.

Mr. LONG. So you don't think it is going to be an issue?

Ms. GREISMAN. As a general matter, no, sir.

Mr. LONG. OK. OK. Being that votes are called and we have got other people to ask questions, Mr. Chairman, I yield back the remainder of my time.

Mr. TERRY. Thank you. Recognize the gentleman from Florida.

Mr. BILIRAKIS. Thank you. Thank you, Mr. Chairman, I appreciate it very much. Question for the panel. American universities are particularly important to the innovation of the economy. I am sure you agree with that. Located in the Tampa Bay area, the University of South Florida is a major research institution that is a worldwide leader in producing university patents and a national leader in producing spinoff companies. Approximately 55 percent of all Federal funded research is conducted by universities. I believe it is in the taxpayers' interest for the research to be developed into products or processes rather than to be underutilized, and I think you probably agree with that, too. The discoveries made at our universities can often be eventually commercialized, but they are patented to protect the investment in development.

There have been concerns that some legislative proposals may inadvertently define the universities as patent trolls. I am confident that this legislation before us does not go that far. With that understanding, will you please discuss how this particular draft bill distinguishes between those who send out large numbers of letters merely seeking payoffs and legitimate large scale patent defenders like our university systems? And we can start with Ms. Greisman, if she would like.

Ms. GREISMAN. I think it directly does in one way by speaking in terms of pattern and practice. Because it is enforced by the FTC Act, as I mentioned earlier, the FTC Act can only act in the public interest, so that is another constraint on what we could do vis—vis enforcing the law, the proposed bill.

Ms. MORGAN. And I would say the enumerated provisions—

Mr. TERRY. Is your microphone on?

Ms. MORGAN. I am sorry. Thank you. The enumerated provisions are going to focus attention on the bad actors, not the people who are legitimately enforcing their patent rights. And the Vermont law that was enacted a year and a half ago specifically addresses the university situation. This one does not, but I think, in any event, the universities are not going to be sending out the kinds of letters that are described here in section 2.

And could I say one more thing about a comment that—

Mr. BILIRAKIS. Sure.

Ms. MORGAN [continuing]. Mr. Mossoff made? He said that there was a Vermont case that struck down compelled speech. It was not compelled speech. It was, in fact, exactly the opposite. It was speech—it was a provision that did not allow certain accurate information, so it is not like what you are dealing with here with deceptive information. It did not allow accurate information to go to

some people while it did to others. It did not allow it to go to marketers as well. It allowed it to go to universities, so I just wanted to clear that up with regard to the Vermont case. Thank you.

Mr. MOSSOFF. In fact, thank you, Ms. Morgan, you preempted my correction. I checked my notes because I was speaking extemporaneously when I answered the question earlier to the Congressman, but yes, it was a preemptive speech that it was struck down. It was a commercial speech case, and so it is a very significant case that indicates that commercial speech is still given much greater scrutiny now than the user—

Mr. TERRY. I understand.

Mr. MOSSOFF [continuing]. Used to receive.

Mr. TERRY. Thank you.

Mr. MOSSOFF. I apologize for that misstatement earlier, but to go back to the question that was presented to the panel. I believe that the question is very well made, Mr. Congressman, because universities, because they license and don't manufacture, are accused of being patent trolls, and for instance, University of Wisconsin, its tech transfer division, WARF, is often listed as one of the "Top 10 Patent Trolls" in lists that you see on the Internet for enforcing its legitimate patent innovation from Wisconsin researchers against infringers.

So I think this is a real concern and that universities and individual inventors have been brought within the scope of this pejorative term "patent troll." And if you don't have actually specified lists, what type of activity you are prohibiting, you risk creating the types of damage to the innovation economy that Mr. Rogers has detailed, I think, quite well with respect to good inventors and original inventors, because a lot of our original large, even large companies today, like Google and Microsoft, Apple, and Hewlett Packard started in garages and were individual inventors. In fact, Google, they were university graduate students at Stanford when they came up with their algorithm. They got a patent on it and received venture capital funding.

Mr. BILIRAKIS. Thank you.

Mr. DAVIS. I agree with you that the bill does a good job in avoiding putting universities into the same category as patent trolls. The statute appropriately does a lot to limit the application of the bill, does a lot to limit its application to patent troll activities and not the legitimate—not for legitimate enforcement behavior. There is a belt, there is suspenders and something else holding up your pants. I mean, there is pattern and practice limitation, there is the bad faith limitation, and there is the user agent model that I think under all those, the universities would probably not be involved in this.

Mr. POTTER. I agree that there are clear distinctions between good actors and bad actors, but I don't want to leave it unstated that universities do have the potential to send out a pattern or practice of deceptive demand letters, and in those contexts, let's remember that universities are taxpayer-funded, patents are a gift or it is earned, but taxpayers are the beneficiary through the government and the PTO of the patent, and we should make sure that everybody is a good actor.

So, I appreciate that, as a general proposition, universities are not in the business of patent trolling, but that doesn't mean we should have clear distinctions if we are defining what is good behavior and what is bad behavior.

Mr. TERRY. The gentleman's time has expired. At this time, I need to enter into a colloquy with the gentleman from Texas. The time for the votes has gone to zero zero, but there are still 288 of us that are not present. If you would like to take over the chair and ask your questions, I would gladly allow that.

Mr. OLSON. I am happy to, sir. And I just have one question. I have got five for the record and submit those guys, thanks for your time.

Mr. TERRY. All right. Go ahead.

Mr. OLSON. My question may be from left field. I know being a baseball fan from Houston, Texas, you got to think what does he know about left field? There are no left fielders in pro-ball for 3 years now.

My question to you, Mr. Potter, is there a role for the State Bar Association to play in cases as the one you describe when the attorney representing the troll declined to engage making concert conversation about his communications?

Mr. POTTER. The answer is maybe, but I can tell you that every small company I have dealt with that has faced this situation just wants to get out this mess and go back to work. They don't want to be then hiring ethics lawyers to go bring charges under the State Bar—in the State Bar Association.

Mr. OLSON. Thank you. Again, I have five questions for the record, four on threshold and one on the rebuttable presumptions. I yield back the balance of my time.

Mr. TERRY. Thank you. Succinct for a Texan.

Mr. OLSON. I can go on longer.

Mr. TERRY. But that does conclude our questions. As Mr. Olson mentioned, we have the ability to submit written questions to you, which I will ask of my colleagues that we have them to our counsel on subcommittee by close of business Wednesday, the 28th, and because we are kind of on a quick timeline, if you would answer them within 10 days of receipt, we would greatly appreciate that, but you are not going to be locked into a room on the 11th day. You may be invited to participate in some meetings, but then now for some wrap-up business.

We have some letters for the record, the National Association of Federal Credit Unions, National Association of Realtors, Office of the Nebraska Attorney General, Main Street Patent Coalition, and by the way, the Office of Nebraska Attorney General John Bruning has his person sitting in the audience today, lawyer Dave Lopez, so thank you for being here as well.

So I ask unanimous consent to submit those four letters. Hearing no objections, they will be part of the record. And that, my friends, ends a rather great hearing, so thank you-all for your participation.

[The information appears at the conclusion of the hearing.]

[Whereupon at 10:53 a.m., the subcommittee was adjourned.]

[Material submitted for inclusion in the record follows:]

PREPARED STATEMENT OF HON. FRED UPTON

I'd like to commend Chairman Terry for his continued work on addressing the growing problem of patent trolls and their practice of sending deceptive demand letters, extorting thousands of dollars out of small businesses. We have heard concerns from a range of businesses, from banks to homebuilders to retailers, that patent trolls are a real threat to their bottom line.

When we embarked upon this effort, it was clear that a balanced and effective solution would require a deliberate approach. On one hand, you have small businesses being intimidated by what sound like legitimate claim letters and deceived into paying large sums of money for licenses they don't need. On the other, you have patent-intensive companies and universities who send demand or licensing letters for legitimate purposes every day.

The importance of intellectual property—and the rights of inventors—was recognized in the earliest days of our country. Article 1, Section 8 of our Constitution declares, "Congress shall have power to promote the progress of science and useful arts, by securing for limited times to authors and inventors the exclusive right to their respective writings and discoveries." The only way to protect one's rights is to put others on notice of your invention. The remedy is up to the patent holder—whether he or she demands an actor cease infringing or pay compensation for the right to continue using an invention.

We know that research and development is the lifeblood of our leading economic sectors, and we don't want to tread on the rights of legitimate companies to engage in legitimate communications protecting their IP rights. We also don't want to make protecting one's rights overly burdensome. Concurrently, we don't want fraudsters to be able to bilk small businesses out of thousands of dollars.

Striking that right balance is why we are here today. We know that some of the concepts in this draft bill are not universally embraced, and I hope that through our dialogue today we can find a path forward. We need a solution that enables rights holders to continue protecting their inventions without overly burdensome regulation while stymying so-called trolls from shaking down hardworking Americans for money to which they have no claim.

And before I yield back, I'd like to take a moment to thank longtime committee staff member Brian McCullough for his many years of dedicated service. Brian began his tenure under Chairman Bliley to work on securities issues, and he has served us well ever since. Brian has been an important voice on some the most important commerce-related issues to come before this committee in the last several years. With his departure, we truly lose a wealth of knowledge—from finance, to consumer protection, to autos and the world of NHTSA—and I want to thank him for his dedicated service and wish him well.



3138 10th Street North
Arlington, VA 22201-2149
703.522.4770 | 800.336.4644
F: 703.524.1082
nafcu@nafcu.org

National Association of Federal Credit Unions | www.nafcu.org

May 20, 2014

The Honorable Lee Terry
Chairman
Subcommittee on Commerce,
Manufacturing, and Trade
House Energy and Commerce Committee
U.S. House of Representatives
Washington, D.C. 20515

The Honorable Jan Schakowsky
Ranking Member
Subcommittee on Commerce,
Manufacturing, and Trade
House Energy and Commerce Committee
U.S. House of Representatives
Washington, D.C. 20515

Re: Ending Abusive Patent Demand Letters

Dear Chairman Terry and Ranking Member Schakowsky:

On behalf of the National Association of Federal Credit Unions (NAFCU), the only trade association exclusively representing the interests of our nation's federal credit unions, I write today in advance of Thursday's subcommittee hearing to review draft legislation to address abusive patent demand letters. On behalf of our member credit unions and the 97 million credit union members across the country, we appreciate the subcommittee's attention to this important matter.

A growing number of credit unions are reporting receipt of demand letters from law firms representing patent assertion entities, claiming patent infringement, with the option to settle or face litigation. These deceptive letters are confusing and misleading as they often allege that the use of everyday technology violates the patent holders' rights. Further, these letters typically state vague or hypothetical theories of infringement, and often overstate or misinterpret the patent in question. Because the cost of litigation is often more expensive than paying a settlement amount, these "patent trolls" use the threat of litigation as leverage to extract payment from the recipient business who settles in lieu of running the risk of a complex and lengthy legal battle.

NAFCU believes a legislative solution is necessary to alter the intimidating business model used by these patent assertion entities and is pleased that the subcommittee is considering legislation to curb these practices. We appreciate your work towards a solution and look forward to working with you as this issue moves through the legislative process. If my staff or I can be of assistance to you, or if you have any questions, please feel free to contact myself, or NAFCU's Director of Legislative Affairs, Jillian Pevo, at 703-842-2836.

Sincerely,

Brad Thaler
Vice President of Legislative Affairs

cc: Members of the Subcommittee on Commerce, Manufacturing, and Trade



Steve Brown, ABR, CRS, GRI, SFR
2014 President

Dale A. Sutton
Chief Executive Officer

**GOVERNMENT AFFAIRS
DIVISION**

Jerry Giovaniello, Senior Vice President
Gary Weaver, Vice President
Joe Ventrone, Vice President
Scott Reiter, Vice President
Jamie Gregori, Deputy Chief Lobbyist

May 21, 2014

The Honorable Lee Terry
Chairman
House Commerce Subcommittee on Commerce,
Manufacturing, and Trade
2266 Rayburn House Office Building
Washington, DC 20510

The Honorable Jan Schakowsky
Ranking Member
House Commerce Subcommittee on Commerce,
Manufacturing, and Trade
2367 Rayburn House Office Building
Washington, DC 20510

Dear Chairman Terry and Ranking Member Schakowsky:

On behalf of the more than one million members of the NATIONAL ASSOCIATION OF REALTORS® (NAR), we wish to thank you for raising the issue of abusive patent demand letters with the House Commerce Subcommittee on Commerce, Manufacturing and Trade. While broad patent reform legislation was passed in the House last year and is currently under consideration in the Senate, abusive demand letters are an NAR priority and we applaud the subcommittee's efforts to enact needed reforms in this area.

REALTORS® have been early adopters of technology and are industry innovators who understand that consumers today are seeking real estate information and services that are fast, convenient and comprehensive. Increasingly, technology innovations are driving the delivery of real estate services and the future of REALTORS® businesses.

As technology users, NAR and several of its members recently received unfair and deceptive demand letters for their use of common business technologies including website drop-down menus and search alert functions. Many REALTORS® also received demand letters for the use of scanner-copiers as part of the "Project Paperless" trolling scheme. Our members know firsthand that "patent trolls" divert significant time and money from their businesses.

Practitioners who regularly license technology in a responsible way indicate that a reasonable demand letter will include the patent number, the real "parties of interest" of the patent, some specifics of alleged infringement, and an offer to negotiate a license to the patent. Moreover, the demand letter will be highly tailored to the specific business utilizing the allegedly infringing product.

Instead, the letters REALTORS® have received generally do not identify the party owning the patent nor do they explain the allegedly infringing behavior. In many cases, a REALTOR® may have to spend several thousand dollars in legal fees just to decipher the vague allegations made in these letters. Under these circumstances, our members are likely to conclude that payment of the "licensing fee" is the most practical option. This situation amounts to legalized extortion.

Without needed reforms that require specific disclosures to increase transparency in patent demand letters and to prohibit unfair and deceptive practices, REALTORS® ability to grow, innovate and better serve modern consumers will be curtailed. We look forward to working with you to create needed reforms to the patent system that will truly promote innovation and expand job creation.

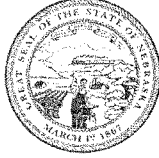
Sincerely,

Steve Brown
2014 President, National Association of REALTORS®



REALTOR® is a registered collective membership mark which may be used only by real estate professionals who are members of the NATIONAL ASSOCIATION OF REALTORS® and subscribe to its strict Code of Ethics.

cc: Members of the House Commerce Subcommittee on Commerce, Manufacturing, and Trade



STATE OF NEBRASKA
Office of the Attorney General
 2115 STATE CAPITOL BUILDING
 LINCOLN, NE 68509-8920
 (402) 471-2682
 TDD (402) 471-2682
 FAX (402) 471-3297 or (402) 471-4725

JON BRUNING
 ATTORNEY GENERAL

May 21, 2014

The Honorable Lee Terry
 Chairman, Subcommittee on Commerce, Manufacturing, and Trade
 Committee on Energy and Commerce
 United States House of Representatives
 2125 Rayburn House Office Building
 Washington, DC 20515

The Honorable Jan Schakowsky
 Ranking Member, Subcommittee on Commerce, Manufacturing, and Trade
 Committee on Energy and Commerce
 United States House of Representatives
 2322A Rayburn House Office Building
 Washington, DC 20515

Re: Discussion Draft on H.R. ____, a bill to enhance federal and state enforcement of
 fraudulent patent demand letters (Hearing held May 22, 2014)

Dear Chairman Terry and Ranking Member Schakowsky:

I write to express my support for your bipartisan efforts to enact legislation to enhance enforcement against unfair, deceptive, and fraudulent patent demand letters. I support state and federal efforts to put an end to so-called "patent trolls" and I believe, generally, that the above-referenced Discussion Draft ("Draft") is a necessary and productive step. However, I have serious concerns regarding the Draft's inclusion of a non-subjective enforcement standard and its pre-emption of state authority.

As a preliminary matter, I proceed from the premise that America's intellectual property enforcement system, though in need of reform, should remain one which readily enables patent holders to engage in good faith enforcement of such patents without undue hurdles or unfair obstacles. I firmly believe in the principle that intellectual property is precisely that – *property* – and that legitimate enforcement of the rights which flow from such property should be protected. Patent trolls, however, have abused America's relatively open system. To protect the integrity of that system while simultaneously protecting consumers and businesses from patent trolls, therefore,

Hon. Terry and Hon. Schakowsky
 May 21, 2014
 Page 2

increased consumer protection tools are necessary at both the federal and state level to address this issue.

My involvement in the fight against deceptive patent demand letters from a consumer protection perspective is extensive. Over the past year, I have received many complaints about unfair and deceptive efforts to license and enforce patents in my state. The targets of these letters – which include individuals, small businesses, start-ups, and nonprofits – often face the difficult choice of paying an expensive and unwarranted licensing fee or risk financially disastrous litigation. Many pay the licensing fee not because the claim has merit but because any other option – getting legal advice or risking litigation – is too expensive. These distorted incentives have caused a significant increase in meritless patent enforcement activity.

I have responded to complaints from my constituents by launching investigations and bringing enforcement actions against demand letter abusers. I have engaged in intense litigation with one of the nation's more notorious consumer-targeting patent trolls. I have partnered with the Nebraska Legislature to introduce a bill to offer state courts guidance in applying existing state consumer protection statutes to actions involving deceptive demand letters. These actions were undertaken pursuant to my obligation to enforce Nebraska's consumer protection laws and based on the principle that Congress had not pre-empted state authority in this area.

The Draft abrogates this principle by expressly pre-empting any state law relating to the sending of patent demand letters, notwithstanding that such letters can be and are used not as legitimate patent enforcement mechanisms, but as vehicles for consumer deception. *See* Draft, § 4(a)(1). Additionally, not only does the Draft eliminate the states' ability to enact legislation specific to bad faith patent demand letters, it places state Attorneys General in a subordinate role to the Federal Trade Commission ("FTC") by forcing them to notify the FTC upon instituting an action under the Draft's authority. *See id.* at § 4(b). This arrangement is inconsistent with principles of Constitutional federalism.

The prosecution of civil actions against actors who engage in unfair, deceptive, or fraudulent conduct is traditionally a responsibility shared equally by state and federal authorities through a system based on concurrent jurisdiction. When an actor commits violations of a state's consumer protection laws within that state, it is the obligation of the state's Attorney General to act swiftly and decisively to enjoin the violations and protect the public. It is beyond doubt that the sending of bad faith patent demand letters constitutes precisely such a violation. The spirit of the Draft appears to affirm that principle. Unfortunately, by carving out a state enforcement exception solely for demand letters that ostensibly implicate legitimate patents, the Draft undermines consumer protection by hampering the ability of state Attorneys General to protect the public.

Additionally, the Draft's enforcement provision could be substantially improved by transforming it into subjective guidance for courts. Specifically, I would encourage

Hon. Terry and Hon. Schakowsky
May 21, 2014
Page 3

you to simplify § 2 by setting forth a direct bar to patent assertions made in bad faith. §§ 2(a)(2), (3) and (4) should remain as guidance factors for courts to consider as evidence of bad faith. This would place the onus on the statute's enforcer to carry its burden of persuasion and build a case against an alleged violator without providing demand letter abusers the possibility of a statutory safe harbor, achieved through pro forma compliance with the Draft's current provisions.

Though I applaud your willingness to tackle this challenge, I urge you to remove the § 4 pre-emption provisions from the Draft and create a subjective enforcement standard in § 2. At minimum, I urge you in the strongest terms to eliminate § 4(b) in its entirety. The provisions therein amount to a serious compromise of the authority of state Attorneys General to protect the public and offend settled notions of concurrent state-federal consumer protection jurisdiction.

I am encouraged by Congress' recent willingness to address bad faith patent demand letters and I urge the Subcommittee to move swiftly to empower the FTC with the tools and resources necessary for it to partner co-equally with the states in this area. I appreciate your time and consideration and look forward to working with you to improve the underlying Draft.

Sincerely,


JON BRUNING
Attorney General of Nebraska

Wednesday, May 21, 2014

The Honorable Lee Terry
Chairman, Subcommittee on Commerce, Manufacturing, and Trade
Committee on Energy and Commerce
United States House of Representatives
Washington, D.C. 20515

The Honorable Jan Schakowsky
Ranking Member, Subcommittee on Commerce, Manufacturing, and Trade
Committee on Energy and Commerce
United States House of Representatives
Washington, D.C. 20515

Dear Mr. Chairman and Ms. Schakowsky,

We commend the leadership of the Subcommittee on Commerce, Manufacturing and Trade and look forward to seeing the committee find a bipartisan solution to the critical problem of PAE demand letters. Businesses threatened by patent assertion entities (PAEs) are encouraged by the support from Chairman Terry and his Subcommittee colleagues by holding a hearing regarding patent trolls. The Chairman's hearing sends the signal to small businesses everywhere that Congress is ready to enact reforms that shield business owners from frivolous patent litigation letters as part of the larger effort to combat patent trolls.

The House already passed a comprehensive patent reform bill at the end of last year and separate patent reform bills are actively under discussion in the Senate. But as today's decision has demonstrated, our work is not finished, which is why we applaud Chairman Terry's push to enact solutions that prevent the wasted resources, unnecessary cost on small business and the general economic speed bumps caused by frivolous patent litigation. The cost of patent trolls on the economy has climbed steadily over the past few years with no sign of letting up.

Small, medium and large businesses continue to hemorrhage money into licensing or court fees, which could otherwise be used to provide more jobs, to innovate, to expand or to simply meet overhead and pay for operations.

Without strong disclosure and transparency requirements united with meaningful litigation reforms, patent trolls' abusive tactics will continue and American business owners will have few means to defend themselves.

The current patent system, intended to protect the rights of inventors and other small businesses has been corrupted and abused by patent trolls that leverage poor quality patents and essentially extort small businesses. Small businesses, which fuel our economy, are then forced into weighing their options between paying costly licensing fees or more expensive legal fees required to fight back.

More transparency around demand letters through greater disclosure and clarity requirements for the patent trolls that send them would help businesses make sense of a demand letter and be better equipped to fight patent litigation. Demand letter transparency is a general concept that enjoys wide-ranging support among the American business community. Right now, Congress has the opportunity to provide thousands of business owners across the country with much-needed relief.

It is clear that the need to prevent vague and deceptive patent demand letters from non-practicing entities enjoys broad bipartisan support and that the urgency of the situation has enough acknowledgement from Congress needed to swiftly go the distance.

We appreciate your consideration of this critical issue and thank you for bringing it to the attention of your colleagues.

Sincerely,

American Apparel & Footwear Association
 American Association of Advertising Agencies
 American Bankers Association
 American Hotel and Lodging Association
 American Gaming Association
 American Society of Home Inspectors
 Application Developers Alliance
 Credit Union National Association
 Direct Marketing Association
 Electronic Frontier Foundation
 The Emob
 Engine
 Food Marketing Institute
 HTC
 Independent Community Bankers of America
 International Franchise Association

The Latino Coalition
 National Association of Convenience Stores
 National Association of Home Builders
 National Association of Federal Credit Unions
 National Association of Realtors
 National Council of Chain Restaurants
 National Grocers Association
 National Retail Federation
 National Restaurant Association
 NTCA -The Rural Broadband Association
 Printing Industries of America
 Public Knowledge
 Retail Industry Leaders Association
 Small Business Majority
 TicketNetwork
 U.S. Travel Association

CC: Members of the House Committee on Energy and Commerce

FRED UPTON, MICHIGAN
CHAIRMAN

HENRY A. WAXMAN, CALIFORNIA
RANKING MEMBER

ONE HUNDRED THIRTEENTH CONGRESS
Congress of the United States
House of Representatives
COMMITTEE ON ENERGY AND COMMERCE
2125 RAYBURN HOUSE OFFICE BUILDING
WASHINGTON, DC 20515-6115
Majority (202) 225-2927
Minority (202) 225-3641

June 4, 2014

Ms. Lois Greisman
Associate Director
Bureau of Consumer Protection
Federal Trade Commission
600 Pennsylvania Avenue
Washington, D.C. 20580


Dear Ms. Greisman,

Thank you for appearing before the Subcommittee on Commerce, Manufacturing, and Trade on Thursday, May 22, 2014 to testify at the hearing focusing on H.R. ___, a bill to enhance federal and state enforcement of fraudulent patent demand letters.

Pursuant to the Rules of the Committee on Energy and Commerce, the hearing record remains open for ten business days to permit Members to submit additional questions for the record, which are attached. The format of your responses to these questions should be as follows: (1) the name of the Member whose question you are addressing, (2) the complete text of the question you are addressing in bold, and (3) your answer to that question in plain text.

To facilitate the printing of the hearing record, please respond to these questions by the close of business on Wednesday, June 18, 2014. Your responses should be e-mailed to the Legislative Clerk in Word format at Kirby.Howard@mail.house.gov and mailed to Kirby Howard, Legislative Clerk, Committee on Energy and Commerce, 2125 Rayburn House Office Building, Washington, D.C. 20515.

Thank you again for your time and effort preparing and delivering testimony before the Subcommittee.

Sincerely,

Lee Terry
Chairman
Subcommittee on Commerce,
Manufacturing, and Trade

cc: Jan Schakowsky, Ranking Member, Subcommittee on Commerce, Manufacturing, and Trade
Attachment

Additional Questions for the Record

Hearing on H.R. __, a bill to enhance federal and state enforcement of fraudulent demand letters
May 22, 2014

The Honorable Lee Terry

1. At the request of the Federal Trade Commission, the discussion draft included language to cover both someone who states and someone who implies that another has infringed a patent. Stakeholders in the regulated community are concerned that this is a vague concept. What does “imply” look like in this context?

The principles that the Commission applies when considering implied claims are discussed in the FTC Policy Statement on Deception, 103 F.T.C. 110, 174 (1984), and in many decisions of the Commission. In evaluating whether a written communication conveys an implied claim, the Commission considers the impression that the communication, considered as a whole, would make on the ordinary reader. Where a communication is directed to a specific audience, the Commission will consider the communication in light of the sophistication of that audience.

There are a number of ways in which an individual who holds or purports to hold a patent might imply infringement without expressly using the words “you are infringing the patent,” such as, for example, by referring to a business’s use of a method or process that is allegedly patented or by stating that the business lacks a license for the patent.

2. You referenced that there is existing case law regarding false threats of litigation under other FTC-enforced statutes. How do you prove an individual’s threats to sue are false?

The truth or falsity of a particular claim always turns on the specific representations made, which may involve, for example, a representation that suit will definitely be filed, that suit will be filed imminently, or that suit will be filed within a specified time period. In considering the truth or falsity of a threat of legal action, courts have considered, depending on the specific representations made, whether the party issuing the threat has actually made a determination to take legal action, whether it has followed through on similar threats in the past, whether it has taken preparatory steps consistent with an intent to follow through on the present threat (such as conducting an appropriate legal review, obtaining necessary counsel, authorizing counsel to proceed, etc.), and whether it has in fact followed through on the present threat.

3. To violate the Act as drafted, an individual must engage in a “pattern or practice” of sending letters in bad faith that are false or deceptive. The FTC enforces violations in other contexts – such as violations of the Fair Credit Reporting Act or of the Telemarketing Sales Rule – where the Commission may obtain civil penalties for a knowing violation that constitutes a pattern or practice. Has the FTC had any difficulties proving a pattern or practice in its enforcement cases in these other contexts? Is there any reason why that standard would cause problems in this context?

To begin, a point of clarification: although the standard to obtain civil penalties under the Fair Credit Reporting Act requires “a knowing violation, which constitutes a pattern or practice of violations,” the same standard does not apply to obtain civil penalties for violations of the Telemarketing Sales Rule, or for violations of other rules or statutes enforced by the Commission. *Compare* 15 U.S.C.

§ 1681(s)(a)(2) (civil penalties for FCRA violations) *with* 15 U.S.C. § 45(m)(1)(A) (civil penalties for violations of FTC rules).

The FCRA standard differs in certain key respects from the use of similar language in the Discussion Draft. Under the FCRA, a showing of the defendant's knowledge and the existence of a "pattern or practice" of violations is not required to establish a violation; such a showing is relevant only to establishing liability for civil penalties. In the Discussion Draft, by contrast, such showings would be required to establish a violation of the proposed Act.

As a practical matter, this means that while the Commission can obtain injunctive relief to halt violations of FCRA without any showing of the defendant's knowledge or a "pattern or practice," the Commission would not be able to obtain injunctive relief to halt violations of the proposed Act without making these additional showings.

While the inclusion of the "pattern or practice" language does create an additional hurdle to enforcement, in the specific context of deceptive demand letters and in the context of the current version of the Discussion Draft, Commission staff believes that the hurdle would not be significant. In the FCRA context, the Commission has a successful record of obtaining civil penalties for conduct that involves a pattern or practice of violations.¹

As noted in its written testimony, however, the Commission has concerns about the proposed requirement of a showing of "knowledge" to establish a violation of the proposed Act. Consumers can be harmed misrepresentations regardless whether the party making the representations knows them to be false. For this reason, when enforcing Section 5 of the FTC Act, the Commission can obtain injunctions to halt deceptive conduct without regard to the defendant's knowledge or intentions. Commission staff does not perceive a compelling reason why consumers should be entitled to less protection in the context of deceptive demand letters than in other contexts, and would strongly recommend removing the "knowledge" requirement.

The Honorable Jan Schakowsky

1. Some stakeholders have expressed concerns that the definitions in the draft are too narrow, and therefore fail to adequately include those who may be the targets of unfair and deceptive demand letters, or those who engage in unfair or deceptive acts or practices with regard to patent demand letters. We have also heard that some of the definitions may cause uncertainty that would affect the ability of the FTC and state attorneys general to enforce the law.
 - a. For example, FTC staff has mentioned a concern with defining "consumer." Please elaborate on that concern. Do you have any concerns that including a definition of "consumer" in the bill would set a bad precedent or could have negative repercussions in any way for the Commission's enforcement authority? Does the specific definition used in the draft bill pose any potential problems for the Commission's enforcement authority? If so, please discuss them.

As explained below in response to part (b), Commission staff has concerns about the term "consumer" as defined and used in the Discussion Draft, as well as the terms "end user" and "systems integrator." In addition to the concerns identified in response to part (b), we are concerned

¹ See, e.g., *United States v. Instant Checkmate, Inc.*, No. 14-675 (S.D. Cal. Apr. 1, 2014) (consent order providing for payment of \$525,000 civil penalty); *United States v. TeleCheck Servs., Inc.*, No. 14-62 (D.D.C. Jan. 17, 2014) (stipulated final order providing for \$3.5 million civil penalty).

that the inclusion of a limited definition of “consumer” in the proposed Act could encourage arguments that, despite the savings clause, similar limitations should apply in the context of enforcement of Section 5 of the FTC Act, which could curtail our ability to effectively prevent unfair and deceptive acts and practices. Because the use of the term is problematic and, in the view of Commission staff, unnecessary, Commission staff recommends removing the term from the proposed Act.

- b. FTC staff mentioned the draft’s limitations on who is defined as a target of these abusive letters. Please elaborate on that concern. The draft limits those who may be the targets or victims of these unfair or deceptive acts or practices to consumers, end users, and systems integrators, a group which is even further limited by the draft bill’s definitions of “consumer,” “end user,” “systems integrator,” or “recipient.” Would these definitions in any way pose potential problems for the Commission’s authority or ability to bring enforcement actions under this proposed law?

Commission staff believes that the proposed Act would be stronger and clearer if the terms “consumer,” “end user,” and “systems integrator” were removed from the Discussion Draft. Commission staff believes that the terms are under-inclusive and likely to complicate litigation.

Commission staff is concerned that the definitions used in the Discussion Draft may be under-inclusive in various respects. For example, the definitions do not clearly protect an individual or business from deceptive representations made in connection with the assertion of a method or process patent. A letter may assert a patent that purportedly covers a process that involves the use of at least two products in combination, such as, for example, a credit card reader and a computer network. Although the letter recipient may think of itself as an “end user” of the process, it is likely that the patent asserter will argue that, because the letter recipient has not “purchase[d] or contract[ed] for purchase” the process in question, the recipient is not a “consumer” or “end user” within the proposed Act’s definitions, nor is it a “systems integrator,” as that definition focuses on software development.

The proposed definitions may compromise effective enforcement of the proposed Act because any patent asserter charged with making deceptive representations will seek to argue that deceived parties did not fall within one of the proposed Act’s protected definitions. In any actions brought to enforce the proposed Act, significant time and effort may be expended on litigating the meaning and application of these terms instead of the truth or falsity of the allegedly deceptive representations.

- c. FTC staff has mentioned a concern with the definition of “recipient.” Please elaborate on that concern. A recipient under the definition in the draft bill is considered not have an “established business relationship with the sender.” Could this language be interpreted in problematic ways? If so, how might it affect the Commission’s ability to enforce the law?

The definition of “recipient” in the Discussion Draft relies on the terms “consumer,” “end user,” and “systems integrator.” For the reasons noted above, Commission staff believes these terms are problematic and unnecessary. The definition of “recipient” also excludes from coverage those who have an “established business relationship” with the “sender.” Commission staff does not perceive a reason to allow deceptive communications to be targeted at those who have an established business relationship with the sender. Moreover, the term “sender” is defined in a

manner that could make the proposed Act more complicated and difficult to enforce.² Because the ordinary meanings of “recipient” and “sender” are sufficient for purposes of the proposed Act, Commission staff would recommend removing the Discussion Draft’s definitions of those terms.

² “Sender” is defined as “a person who has the right to license or enforce the patent at the time the communication is sent, or a person who represents such person, or both.”

FRED UPTON, MICHIGAN
CHAIRMAN

HENRY A. WAXMAN, CALIFORNIA
RANKING MEMBER

ONE HUNDRED THIRTEENTH CONGRESS
Congress of the United States
House of Representatives
COMMITTEE ON ENERGY AND COMMERCE
2125 RAYBURN HOUSE OFFICE BUILDING
WASHINGTON, DC 20515-6115
Majority (202) 225-2927
Minority (202) 225-3641

June 4, 2014

Ms. Wendy Morgan
Chief of the Public Protection Division
Office of the Attorney General of Vermont
109 State Street
Montpelier, VT 05609-1001

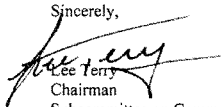
Dear Ms. Morgan,

Thank you for appearing before the Subcommittee on Commerce, Manufacturing, and Trade on Thursday, May 22, 2014 to testify at the hearing focusing on H.R. ___, a bill to enhance federal and state enforcement of fraudulent patent demand letters.

Pursuant to the Rules of the Committee on Energy and Commerce, the hearing record remains open for ten business days to permit Members to submit additional questions for the record, which are attached. The format of your responses to these questions should be as follows: (1) the name of the Member whose question you are addressing, (2) the complete text of the question you are addressing in bold, and (3) your answer to that question in plain text.

To facilitate the printing of the hearing record, please respond to these questions by the close of business on Wednesday, June 18, 2014. Your responses should be e-mailed to the Legislative Clerk in Word format at Kirby.Howard@mail.house.gov and mailed to Kirby Howard, Legislative Clerk, Committee on Energy and Commerce, 2125 Rayburn House Office Building, Washington, D.C. 20515.

Thank you again for your time and effort preparing and delivering testimony before the Subcommittee.

Sincerely,

Lee Terry
Chairman
Subcommittee on Commerce,
Manufacturing, and Trade

cc: Jan Schakowsky, Ranking Member, Subcommittee on Commerce, Manufacturing, and Trade
Attachment

Answers of Wendy Morgan to Additional Questions of the Subcommittee on Commerce, Manufacturing, and Trade on H.R. __, a bill to enhance federal and state enforcement of fraudulent patent demand letters (testimony heard Thursday, May 22, 2014).

The Honorable Jan Schakowsky

1. At the Subcommittee hearing on May 22, 2014, the witness panel discussed the constitutionality of the transparency provisions in Section 2(a)(4) of the draft bill under the First Amendment, based on “compelled speech” case law. In raising these concerns, a number of cases were mentioned, including a Supreme Court case involving the state of Vermont that dealt with restrictions on commercial speech.
 - a. Please discuss the Court’s reasoning in the Vermont case and any implications that case may have for transparency requirements in the draft bill.

Contrary to some of the testimony offered at the hearing, the Supreme Court’s decision in *Sorrell v. IMS Health Inc.*, 131 S. Ct. 2653 (2011), has little if any relevance to the transparency provisions in the draft bill. The Court in *Sorrell* struck down restrictions on speech. The case had nothing to do with transparency or disclosure requirements of this kind. Specifically, *Sorrell* involved a constitutional challenge to a Vermont law that “restrict[ed] the sale, disclosure, and use of pharmacy records that reveal the prescribing practices of individual doctors.” *Id.* at 2659. The Court concluded that the law “enacts content- and speaker-based restrictions,” burdening “disfavored speech by disfavored speakers.” *Id.* at 2663. The Court applied heightened scrutiny to this restriction, finding that the law “impose[d] more than an incidental burden on protected expression.” *Id.* at 2665. The State was, therefore, required to “show at least that the statute directly advances a substantial governmental interest and that the measure [was] drawn to achieve that interest.” *Id.* at 2667-68. The Court held that Vermont did not make a sufficient showing to meet that test. *Id.* at 2672.

In short, the law that was challenged in *Sorrell* restricted speech. The transparency provisions set forth in Section 2(a)(4) of the draft bill do not restrict speech but rather require disclosure of accurate, uncontroversial factual information. The Court in *Sorrell* acknowledged that “[f]acts, after all, are the beginning point for much of the speech that is most essential to advance human knowledge and to conduct human affairs.” *Sorrell*, 131 S. Ct. at 2667. Disclosure requirements may also be challenged under the First Amendment, as compelled speech, but the legal standards are substantially different. The Court’s reasoning in *Sorrell* would not be directly applicable to the disclosure requirements in the draft bill.

- b. While a First Amendment compelled speech concern was raised at the hearing, is there case law that would support mandatory disclosures such as the types that are included in Section 2(a)(4) of the draft bill? Please explain.

Yes. The Supreme Court and federal appellate courts have upheld disclosure requirements for commercial speech and for campaign-related political speech.

The Supreme Court has concluded that the “right of freedom of thought protected by the First Amendment against state action includes both the right to speak freely and the right to refrain from speaking at all.” *Wooley v. Maynard*, 430 U.S. 705, 714 (1977). However, with respect to

commercial speech, the Court has “emphasized that because disclosure requirements trench much more narrowly on an advertiser’s interests than do flat prohibitions on speech, ‘warning[s] or disclaimer[s] might be appropriately required . . . in order to dissipate the possibility of consumer confusion or deception.’” *Zauderer v. Office of Disciplinary Counsel of Sup. Ct. of Ohio*, 471 U.S. 626, 651 (1985) (citing *In re R.M.J.*, 455 U.S. 191, 201 (1982)). It is not necessary to show that actual deception has occurred if there is evidence “adequate to establish that the likelihood of deception in this case ‘is hardly a speculative one.’” *Milavetz, Gallop & Milavetz, P.A. v. United States*, 559 U.S. 229, 251 (2010) (citation omitted). The disclosures set forth in Section 2(a)(4) of the draft bill provide information that would eliminate the deception that occurs when patent holders omit material information necessary for recipients to make licensing and litigation decisions, such as the owner of the patent, the party entitled to enforce the patent, and the claims of the patent that are allegedly infringed.

The First and Second Circuits have concluded that, under *Zauderer*, compelled disclosures in commercial speech are permissible when the disclosure serves an important government interest. See *Pharm. Care Mgmt. Ass’n v. Rowe*, 429 F.3d 294, 310 n.8 (1st Cir. 2005) (declining to limit the application of *Zauderer* “to potentially deceptive advertising directed at consumers” and considering state’s “interest in ensuring that its citizens receive the best and most cost-effective health care possible”); *Nat’l Elec. Mfgs. Ass’n v. Sorrell*, 272 F.3d 104, 107 n.1 (2d Cir. 2001) (considering government interest in informing consumers of products containing mercury in order to allow for proper disposal so that mercury does not become part of solid waste or wastewater). The Second Circuit, applying *Zauderer*, explained that “[c]ommercial disclosure requirements are treated differently from restrictions on commercial speech because mandated disclosure of accurate, factual, commercial information does not offend the core First Amendment values of promoting efficient exchange of information or protecting individual liberty interests.” *Nat’l Elec. Mfgs.*, 272 F.3d at 113-14. In fact, the court explained that “[s]uch disclosure furthers, rather than hinders, the First Amendment goal of the discovery of truth and contributes to the efficiency of the ‘marketplace of ideas.’” *Id.* at 114.

Required disclosures have even been upheld in circumstances that involve highly protected speech, such as political speech. The Supreme Court has upheld disclosure requirements with respect to campaign contributions. *Citizens United v. Fed. Election Comm’n*, 558 U.S. 310, 366 (2010). The Court explained that “[d]isclaimer and disclosure requirements may burden the ability to speak, but they impose no ceiling on campaign-related activities, and do not prevent anyone from speaking.” *Id.* (quotations omitted). Despite acknowledging that “[t]he First Amendment has its fullest and most urgent application to speech uttered during a campaign for political office,” *id.* at 339, the “transparency” arising from mandated disclosure of the person making the speech “enables the electorate to make informed decisions and give proper weight to different speakers and messages.” *Id.* at 371. In the electoral context the Supreme Court has subjected disclosure requirements to “exacting scrutiny,” requiring “a ‘substantial relation’ between the disclosure requirement and a ‘sufficiently important’ government interest.” See *John Doe No. 1 v. Reed*, 561 U.S. 186, 196 (2010) (quotations omitted).

The disclosure requirements in Section 2(a)(4) of the draft bill are limited and not burdensome. They relate to the enforcement of a governmentally created right of patent holders to enforce their patents. They promote the significant governmental interest of assuring that recipients of these letters are not deceived and that licensing and litigation decisions can be made with adequate information.

2. Some stakeholders have expressed concerns that the definitions of “consumer,” “end user,” and “systems integrator,” as defined in the draft bill, are too narrow, and therefore fail to adequately include those who may be the targets of unfair or deceptive demand letters.

Does the use of the terms “consumer,” “end user,” and “systems integrator,” as defined in the draft bill, adequately encompass the universe of persons or businesses that are the targets of abusive demand letters? Should the definitions be altered or broadened in some way?

The definitions “consumer” and “end user” generally encompass the universe of persons that have complained to the Vermont Attorney General’s Office regarding the receipt of unfair and deceptive patent demand letters.

The definition of “systems integrator,” could be broadened to better address developers and other entrepreneurs that incorporate retail software into their products. Currently, “systems integrator” is limited to “a person who develops or contracts for the development of a website or mobile application that incorporates retail software or services.” This limits the applicability to website and mobile application developers, which may exclude some software developers and may exclude developers in the future that work in different platforms. We recommend modifying the definition to include “a person who incorporates retail software or services (including website, network, or analytics services) into products or services intended for direct sale or license to consumers or end users if the communication relates to the incorporated retail software or service.”

FRED UPTON, MICHIGAN
CHAIRMAN

HENRY A. WAXMAN, CALIFORNIA
RANKING MEMBER

ONE HUNDRED THIRTEENTH CONGRESS
Congress of the United States
House of Representatives
COMMITTEE ON ENERGY AND COMMERCE
2125 RAYBURN HOUSE OFFICE BUILDING
WASHINGTON, DC 20515-6115
Majority (202) 225-2927
Minority (202) 225-3641

June 4, 2014

Mr. Jon Potter
President and Co-Founder
Application Developers Alliance
1025 F Street, N.W., Suite 720
Washington, D.C. 20004

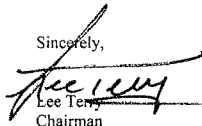
Dear Mr. Potter,

Thank you for appearing before the Subcommittee on Commerce, Manufacturing, and Trade on Thursday, May 22, 2014 to testify at the hearing focusing on H.R. ___, a bill to enhance federal and state enforcement of fraudulent patent demand letters.

Pursuant to the Rules of the Committee on Energy and Commerce, the hearing record remains open for ten business days to permit Members to submit additional questions for the record, which are attached. The format of your responses to these questions should be as follows: (1) the name of the Member whose question you are addressing, (2) the complete text of the question you are addressing in bold, and (3) your answer to that question in plain text.

To facilitate the printing of the hearing record, please respond to these questions by the close of business on Wednesday, June 18, 2014. Your responses should be e-mailed to the Legislative Clerk in Word format at Kirby.Howard@mail.house.gov and mailed to Kirby Howard, Legislative Clerk, Committee on Energy and Commerce, 2125 Rayburn House Office Building, Washington, D.C. 20515.

Thank you again for your time and effort preparing and delivering testimony before the Subcommittee.

Sincerely,

Lee Terry
Chairman
Subcommittee on Commerce,
Manufacturing, and Trade

cc: Jan Schakowsky, Ranking Member, Subcommittee on Commerce, Manufacturing, and Trade
Attachment



June 18, 2014

TO: Kirby Howard
Legislative Clerk
Committee on Energy and Commerce

FROM: Jon Potter
Application Developers Alliance

RE: Additional Q&A for the Record – May 22nd Energy and Commerce Subcommittee on Consumer Protection, Trade, & Manufacturing Hearing on Abusive Demand Letters

The Honorable Lee Terry

1. **Both you and Mr. Davis, expressed concerns regarding the current definition of "systems integrator." While the definition in the bill was a blend of suggested language, the purpose of its addition to the bill is to be more inclusive. Can you give us examples of who would be excluded from the bill's protections as a result of the definition? Would it be better to not have a "systems integrator" definition at all?**

Irrespective of whether a developer is incorporating third-party software in a product or developing custom software from scratch, all developers deserve protection from deceptive and abusive demand letters. By defining "systems integrator[s]" who are protected against demand letter fraud (albeit in an effort to be inclusive), the discussion draft distributed prior to the hearing necessarily leaves other developers unprotected against demand letter fraud. In contrast, the Alliance urges the Committee to protect all citizens against fraud, which we believe would be accomplished if the definition were eliminated.

2. **In the examples provided to the Committee, the questionable demand letters often reference only a handful of patents, but we've heard that in sophisticated technology cases the claims can often number in the hundreds or more. Mr. Rogers argued that in requiring all disclosures in such cases, if even possible, the volume of the communications could become overly burdensome to both the sender and the recipient. Additionally, industries that are otherwise not interested in this debate have expressed the view that requiring a claim chart would cause them to care about this bill and oppose it. How do we reconcile these competing interests?**

The purpose of a demand letter is simple: to put the letter recipient on notice that infringement of one or more patents is occurring, and that a license and royalties are obligated. Trolls intentionally do not include clear and specific information about the relevant patent(s), claim(s)

and offending activities or functionalities because trolls do not want to inform – they want to threaten.

Good faith owners of high-quality patents do not send demand letters without careful research that determines with some modicum of certainty that infringement is occurring. Summarizing and including that research in demand letters is simply not burdensome.

With regard to the volume of information that is required when multiple patents are allegedly infringed – it is the patent owner's decision whether to assert that a party is infringing one patent or one hundred patents, or one claim or dozens of claims. But – again – requiring the demand letter sender to articulate the basis of each infringement assertion (presuming there is a good faith basis for each assertion) seems quite minimal, ordinary and justified.

If there is no articulable basis for each specific assertion, then the assertion simply cannot be considered justified by neutral observers and the letter recipient cannot be considered to have received notice of an alleged infringement. Unsupported infringement assertions are more likely to be fraudulent and abusive, rather than good faith efforts to secure a justifiable license.

FRED UPTON, MICHIGAN
CHAIRMAN

HENRY A. WAXMAN, CALIFORNIA
RANKING MEMBER

ONE HUNDRED THIRTEENTH CONGRESS
Congress of the United States
House of Representatives
COMMITTEE ON ENERGY AND COMMERCE
2125 RAYBURN HOUSE OFFICE BUILDING
WASHINGTON, DC 20515-6115
Majority (202) 225-2027
Minority (202) 225-3641

June 4, 2014

Mr. Alex Rogers
Senior Vice President for Litigation
Qualcomm Incorporated
5775 Morehouse Drive
San Diego, CA 92121-1714

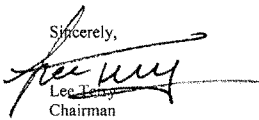
Dear Mr. Rogers,

Thank you for appearing before the Subcommittee on Commerce, Manufacturing, and Trade on Thursday, May 22, 2014 to testify at the hearing focusing on H.R. ___, a bill to enhance federal and state enforcement of fraudulent patent demand letters.

Pursuant to the Rules of the Committee on Energy and Commerce, the hearing record remains open for ten business days to permit Members to submit additional questions for the record, which are attached. The format of your responses to these questions should be as follows: (1) the name of the Member whose question you are addressing, (2) the complete text of the question you are addressing in bold, and (3) your answer to that question in plain text.

To facilitate the printing of the hearing record, please respond to these questions by the close of business on Wednesday, June 18, 2014. Your responses should be e-mailed to the Legislative Clerk in Word format at Kirby.Howard@mail.house.gov and mailed to Kirby Howard, Legislative Clerk, Committee on Energy and Commerce, 2125 Rayburn House Office Building, Washington, D.C. 20515.

Thank you again for your time and effort preparing and delivering testimony before the Subcommittee.

Sincerely,

Lee Terry
Chairman
Subcommittee on Commerce,
Manufacturing, and Trade

cc: Jan Schakowsky, Ranking Member, Subcommittee on Commerce, Manufacturing, and Trade
Attachment

Responses of Alex Rogers Senior Vice President, Legal Counsel, Qualcomm, Incorporated to
Additional Questions for the Record
submitted by Subcommittee on Commerce, Manufacturing, and Trade

The Honorable Lee Terry

1. A number of stakeholders have commented on the complications created by defining the recipients intended to be covered by this bill, whether they be consumers sitting in their home, small businesses, or the middle man intended to be captured by “systems integrator.” If you have the threshold of “pattern and practice,” and you have the scienter requirement of “bad faith” in order to avoid penalties for unintentional behavior, and you have the rebuttable presumption to avoid a technical violation of the disclosure requirements, do you need the definitions to avoid capturing behavior between sophisticated companies?

The “pattern or practice” and “bad faith” requirements of the bill are essential safeguards. Their inclusion in the bill is necessary to distinguish between deceptive shakedown scenarios warranting FTC or state attorney general enforcement and legitimate individualized patent correspondence between sophisticated parties. The recipient categories also serve an important purpose. Limiting the bill to communications sent to defined groups of recipients likely to lack a familiarity with patent law or the resources necessary to evaluate and respond to a patent demand letter furthers the goal of protecting those most vulnerable to abusive demand letters while reducing the risk that either the FTC or state attorneys general will be drawn into individual disputes between patent owners and potential licensees or alleged infringers. Without this limitation, there is a risk that large sophisticated companies may try to use the law, and the threat of the FTC’s enforcement authority under it, in a manner not intended by Members of Congress. With this limitation, the bill fully serves the intended purpose of preventing and remedying harm to recipients from abusive demand letters. If Members of Congress decide to eliminate the recipient categories, enforcement should be limited to individual consumers and small businesses, consistent with the FTC’s historical practice.

2. With respect to the definition of “systems integrator,” what would be the effect of removing the limitation to websites and mobile applications? What are specific examples of the kinds of companies that would then be considered a systems integrator that would cause you concern?

As your first question above indicates, it is my understanding that the term “systems integrator” is meant to cover the “middle man” who is similarly situated with a consumer or end user in terms of his or her ability to assess and respond to a demand letter, but may not fall within either of those categories as they are defined in the bill. An example of such a “middle man” is a small business that integrates the software product of another into a website or mobile application it is developing for another small business, like a coffee shop. Qualcomm does not oppose the inclusion of a recipient category intended to capture this “middle man” concept.

There may be a way to change the definition of “systems integrator” to capture the idea of a “middle man” without making express reference to websites and mobile applications. However, simply eliminating the website and mobile application language from the “systems integrator” definition in the Committee May 15, 2014 discussion draft would result in an expansive definition, which would encompass a wide array of consumer product manufacturers, electronics, medical devices, and even makers of heavy manufacturing equipment or systems. Software products are incorporated into an enormous array of commercial products. Accordingly, without a narrow and well-tailored definition, virtually any company that incorporates software into a product would fall within the definition of a systems integrator.

3. With respect to the definition of “systems integrator,” what is the effect of limiting the definition to people who “utilize a finished or off-the-shelf software product?” Who and what kinds of products does that exclude?

The effect of limiting the definition of “systems integrator” to people who utilize a finished or off-the-shelf software product is to (1) make the definition of “systems integrator” sufficiently robust as to cover those small “middle men” downstream in the supply chain in need of the same protections from demand letters that consumers and end users do, (2) without sweeping in large sophisticated developers of software, websites, or computer applications. The latter are uniquely knowledgeable about the relevant technology and unlikely to fall victim to deceptive demand letters. If the definition of systems integrator is not limited to people who utilize finished or off-the-shelf software products, it would cover all developers of software products. This would include an expansive list of high-profile companies well-versed in sending and receiving patent-related communications.

4. Mr. Davis recommended we require the disclosure of the real party in interest. First, I understand that non-disclosure agreements (NDAs) are often utilized that would prevent the disclosure of such information. Is that true, and if so, what is the purpose of these NDAs? Is there precedent in any other area of the law where Congress has forced the disclosure of information protected by otherwise legal NDAs?

Responding to this inquiry requires an understanding of what information would need to be disclosed under a real party in interest provision, as the term “real party in interest” does not have a defined or understood meaning in this context. Mr. Davis’s written testimony does not provide details regarding what his proposed real party in interest disclosure would entail. To the extent a real party in interest provision would require disclosure of the patent holder’s parent company or ultimate parent company, it is unlikely that an NDA would prevent disclosure of the existing parent-subsidiary relationship.

However, if a party were required to disclose more in-depth information (for example, the identity of any person with a financial interest in the patent being asserted), the disclosure could very well implicate information protected by an NDA. NDAs are often part of legitimate patent assignment, royalty, or licensing

agreements. NDAs are also frequently part of joint venture or partnership agreements between technology companies that come together to develop or commercialize new technologies, as such arrangements can involve existing, pending, or anticipated patents. In addition to the confidentiality concerns, an overly broad real party disclosure requirement would be extremely burdensome for the patentee.

5. Mr. Potter and others have recommended that the patent owner be required to describe the patent claims in a demand letter. Is this feasible? If not, why not?

Such a disclosure requirement may not be feasible for many patent holders. For small patent holders, particularly independent inventors, start-ups and those lacking extensive resources to devote to patent enforcement, the burden of identifying all allegedly infringing claims in a demand letter would be enormous, expensive, and impractical, and could impair their ability to enforce their intellectual property rights. The burden would be highest on the most prolific small inventors, and that burden would outweigh the potential benefit to the recipients. In addition, it would not be feasible for larger companies with significant patent portfolios to identify all allegedly infringing patent claims. Licensing negotiations involving a patent portfolio can implicate hundreds or thousands of patents and numerous different devices, product models, or manufacturing processes.

The unintended consequence of such a disclosure requirement may be to discourage parties from reaching private, pre-suit resolutions in patent disputes. Indeed, if a patentee must invest the considerable time and expense necessary to identify in a demand letter each allegedly infringed patent claim and provide a limitation-by-limitation analysis of how those claims are infringed, it will change the calculus regarding whether to attempt to resolve the dispute without resorting to litigation or simply to file suit for infringement. The impact could be to lead more patentees to the courthouse, as well as discouraging the overall enforcement of legitimate patent rights.